

H.R. 5828, THE UNIVERSAL SERVICE REFORM ACT OF 2010

HEARING BEFORE THE SUBCOMMITTEE ON COMMUNICATIONS, TECHNOLOGY, AND THE INTERNET OF THE COMMITTEE ON ENERGY AND COMMERCE HOUSE OF REPRESENTATIVES ONE HUNDRED ELEVENTH CONGRESS SECOND SESSION

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H.R. 5828, THE UNIVERSAL SERVICE REFORM ACT OF 2010

THURSDAY, SEPTEMBER 16, 2010

HOUSE OF REPRESENTATIVES,
SUBCOMMITTEE ON COMMUNICATIONS, TECHNOLOGY,
AND THE INTERNET,
COMMITTEE ON ENERGY AND COMMERCE,
Washington, DC.

The subcommittee met, pursuant to notice, at 10:04 a.m., in Room 2322, Rayburn House Office Building, Hon. Rick Boucher [chairman of the subcommittee] presiding.

Present: Representatives Boucher, Stupak, Doyle, Inslee, Matsui, Christensen, Castor, Murphy, Space, McNerney, Waxman (ex officio), Stearns, Terry, Blackburn, and Latta.

Staff Present: Amy Levine, Counsel; Greg Guice, Counsel; Sarah Fisher, Special Assistant; Josh Bercu, Intern; Tim Powderly, Counsel; Neil Fried, Minority Counsel; William Carty, Minority Professional Staff Member; and Jeanne Neal, Minority Research Analyst.

OPENING STATEMENT OF HON. RICK BOUCHER, A REPRESENTATIVE IN CONGRESS FROM THE COMMONWEALTH OF VIRGINIA

Mr. BOUCHER. The subcommittee will come to order.

This morning's hearing is a legislative hearing on H.R. 5828, the "Universal Service Reform Act of 2010." The bill is a comprehensive reform of the Universal Service High-Cost Fund, and the measure before us this morning has been revised in various respects based on recommendations we have received during and following the subcommittee's last hearing on the legislation.

H.R. 5828 is the product of a bipartisan effort that I undertook, beginning several years ago, with our subcommittee colleague, the gentleman from Nebraska, Mr. Terry. We have benefited from the advice and suggestions of other members of our subcommittee, members of the full committee, and a broad range, including dozens of interested parties.

We have also conducted extensive conversations with a very broad audience. We have achieved consensus among a broad range of competing interests, and I think you will see that consensus clearly reflected here today in the testimony of our witnesses. You will hear this morning endorsements for the legislation from companies and trade associations that have long been in basic disagreement about the High-Cost Fund and how it should be reformed.

Net contributors into the fund, such as AT&T and Verizon, are today in agreement with net beneficiaries from the fund, such as rural carriers represented by NTCA, OPATSCO, and WTA, that H.R. 5828 in the form in which it appears before the committee today should be approved. We also have endorsements for the legislation from Qwest, CenturyLink, Frontier, Vonage, the National Cable and Telecommunications Association, and USTelecom, reflecting a truly broad consensus.

The High-Cost Fund, which assures affordable rural telephone service, has come under increasing pressure, and comprehensive reform to ensure its continued stability is urgently needed. New technologies and new business plans are combining to diminish the long-distance revenues that historically have been the base of support for universal service.

The current USF contribution rate stands near its highest level ever, at more than 13 percent. In October, that rate will dip slightly to 12.9 percent, but all signs point to double-digit contribution rates going forward in the absence of comprehensive reform.

In addition, the Universal Service Fund is clearly outdated, as it supports only voice-based telephone service. Our legislation extends the program to broadband and, in fact, contains a mandate that carriers deploy broadband throughout their service territories as a condition of their continued receipt of universal service funding.

Many of the Federal Communications Commission's National Broadband Plan recommendations are reflected in our legislation. It gives the FCC the statutory authority that it needs to carry out its universal service goals. In addition, the legislation expands the fund's contribution base by assessing intrastate as well interstate and international revenues, and it requires that providers of broadband connections make a contribution into the fund.

The bill grants the FCC the authority to implement competitive bidding for distributions of fund moneys to wireless carriers, with a limit of two winners per service area, avoiding the potential legal challenges from those who argue that competitive bidding does not comport with existing statutory universal service principles. Removing regulatory uncertainty in these areas will avoid the protracted litigation regarding commission authority that almost certainly will come, particularly in the wake of the D.C. Circuit's Comcast decision that further circumscribed FCC statutory authority. Passing this bill will allow for expeditious reform of the Universal Service Fund through appropriate action at the Federal Communications Commission.

Our legislation would also direct the FCC to adopt a new cost model for USF support based on the provision of both voice and broadband service, while also limiting growth of the fund by providing that contribution burdens on consumers may not unreasonably increase.

As I mentioned earlier, we mandate that all recipients of universal service support offer broadband throughout their service areas at minimum speeds that would be adjusted by the Commission from time to time. And we fully anticipate that these speeds will increase over time as technology permits.

Other elements of our measure include fixing the phantom traffic problem by requiring that carriers pass through call identification

information so that the terminating carriers know to whom to send the bill for call originations. We eliminate traffic pumping by prohibiting carriers from sharing access charge revenue with third parties where those third parties offer free or reduced-cost services.

We make permanent the Anti-Deficiency Act exemption for USF so that an annual appropriations rider will no longer be necessary in order to continue financing for the fund. And we deny universal service support in areas where there is competition in the offering of voice-based telephone service, a new departure for the Universal Service Fund.

The bill modernizes a program that ensures the availability of communications connections to millions of Americans, benefiting not just the rural residents who live in the high-cost areas but benefiting our entire Nation. We are a stronger Nation when we are all connected through telecommunications services. Having rural America connected is essential for efficient nationwide communications and gives Internet-based businesses, for example, access to millions of homes that would be disconnected as customers to these Internet-based companies if the Universal Service Fund did not exist and was not viable.

I want to thank the Members, their staffs, and the dozens of stakeholders who have participated with us in drafting a reform measure that, as the testimony of our witnesses today will reveal, enjoys a true consensus and very broad-based support.

I want to thank our witnesses for taking the time to join us here in the wake of their participation with us in formulating this measure. We very much look forward to your testimony.

That concludes my opening statement. I am pleased now to recognize the ranking Republican member of our subcommittee, the gentleman from Florida, Mr. Stearns.

[The prepared statement of Mr. Boucher follows:]

STATEMENT OF CONGRESSMAN RICK BOUCHER

**Subcommittee on Communications, Technology and the Internet Hearing
H.R. 5828, the Universal Service Reform Act of 2010**

September 16, 2010

The subcommittee will come to order.

This morning's hearing is a legislative hearing on H.R. 5828, the Universal Service Reform Act of 2010.

The bill is a comprehensive reform of the Universal Service High Cost Fund, and the measure before us this morning has been revised in various respects based on recommendations we have received during and following the subcommittee's last hearing on the legislation.

H.R. 5828 is the product of a bipartisan effort I undertook several years ago with our subcommittee colleague, the gentleman from Nebraska, Mr. Terry. We have benefitted from the advice and suggestions of many other members on a bipartisan basis.

We have also conducted extensive conversations with dozens of stakeholder groups, and we have achieved consensus among a broad range of competing interests.

You will hear this morning endorsements for the legislation from companies and trade associations that have long been in basic disagreement about how the High Cost Fund should be reformed.

Net contributors into the Fund, such as AT&T and Verizon, are today in agreement with net beneficiaries of the Fund, such as rural carriers represented by NTCA, OPASTCO and WTA, that H.R. 5828 in the form in which it is before the committee should be approved.

We also have endorsements for the legislation from Qwest, CenturyLink, Frontier, Vonage, the National Cable and Telecommunications Association, and USTelecom, reflecting a truly broad consensus.

The High Cost Fund, which assures affordable rural telephone service, has come under increasing pressure, and comprehensive reform to ensure its continued stability is urgently needed. New technologies and new business plans are combining to diminish the long-distance revenues that have historically been relied upon to support USF. The current USF contribution rate stands near its highest level ever of more than 13 percent. In October, it will dip slightly to 12.9 percent, but all signs point to continued double-digit contribution rates after that unless reform occurs.

In addition, the Universal Service Fund is outdated, as it supports only the provision of traditional voice telephone service. Our legislation extends the program to broadband.

Many of the FCC's National Broadband Plan recommendations are reflected in our legislation. It gives the FCC the statutory authority it needs to carry out its universal service goals. In addition, the legislation:

- Expands the Fund's contribution base by assessing intrastate, as well as interstate and international, revenues and requires that providers of broadband connections pay into the Fund.
- We grant the FCC the authority to implement competitive bidding for distributions to wireless carriers, with a limit of two winners per service area, avoiding potential legal challenges from those who argue that competitive bidding does not comport with existing statutory Universal Service principles.

Removing regulatory uncertainty in these areas will avoid protracted litigation regarding Commission authority, particularly in the wake of the D.C. Circuit's *Comcast* decision, and allow for expeditious reform of the Universal Service program.

Our legislation would also direct the FCC to adopt a new cost model for USF support based on the provision of both voice and broadband service, while also limiting growth of the Fund by providing that the contribution burden on consumers may not unreasonably increase.

We mandate that all recipients of USF support offer broadband throughout their service areas, at minimum speeds established by the FCC. These required data rates will increase over time.

Other elements in our measure include fixing the phantom traffic problem by requiring carriers to pass through call identification information, eliminating traffic pumping by prohibiting carriers from sharing access charge revenue with third parties that offer free or reduced-cost services, making permanent the Anti-Deficiency Act exemption for USF, so that an annual appropriations rider is no longer required for that purpose, and denying USF support in areas where there is competition in voice telephone service.

The bill modernizes a program that ensures the availability of communications connections to millions of Americans, benefitting not just the rural residents who live in high-cost areas, but benefitting the entire nation. We are a stronger nation when we are all connected through telecommunications.

Having rural America connected is essential for efficient nationwide communications and gives Internet-based businesses access to millions of homes that would be disconnected in the absence of this program.

I want to thank the members, their staffs, and the dozens of stakeholders who have participated with us in drafting a reform measure which reflects a broad consensus.

OPENING STATEMENT OF HON. CLIFF STEARNS, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Mr. STEARNS. Good morning. And thank you, Mr. Chairman.

I just apologize, as I am sure you also agree, to the limited space here, and I apologize to the people who are standing. We are not in the main room because there is a health markup on 21 bills, from H.R. 211 to H.R. 6110. I am sure it is pretty important, but considering everything, we are sorry that we don't have more room for you.

But, Mr. Chairman, I want to thank all of you, thank you particularly for having this important legislative hearing on the "Universal Service Reform Act of 2010." Also, I would like to commend my colleague, Mr. Terry, for his steadfast hard work in developing this legislation. You both received comments from many of us and have taken those into consideration.

Reforming the broken Universal Service Fund I think is a top priority for everybody in this room. There is a bipartisan consensus, too, that the fund is broken. We can probably all agree that the system is fraught with waste, fraud, and abuse. A major overhaul is necessary. The question before us this morning is, what is the appropriate goal to accomplish this program and how do we achieve it?

My colleagues, the 1996 Telecom Act codified universal service, but the concept goes back decades earlier to a time when there was really only one phone company. Now, the landscape looks a whole lot different, yet the fund is still administered by outdated rules. So, accordingly, there is a need to reform the program away from subsidies that may no longer be necessary as technology and services improve and become more widespread. Instead, we need to move towards a solution that ensures the goals of universal service but minimizes consumer cost. Throwing additional money at this crumbling program I think makes little sense.

Nearly everyone in the country has access to phone service, and we have more competition and better technology than ever before. Yet, instead of shrinking the Universal Service Fund, it has ballooned to more than \$8 billion a year, about twice what it was in 2000. Approximately \$4.5 billion of that comes from the high-cost program's subsidies to rural carriers, more than three times the \$1.3 billion spent on that program in 1997.

And when the price tag for universal service goes up, subscribers, customers bear the burden. The FCC projects that almost 13 percent of the monthly long distance bill in the fourth quarter of 2010 will be universal service fees, up from 5.7 percent in 2000.

According to the FCC, however, the bill, as introduced—and this is their words—"could substantially increase the size of the fund." Among the reasons are provisions expanding the fund to broadband without—without—imposing a cap on the fund or ensuring sufficient offsetting savings.

We should not support any Universal Service Fund reform legislation that is absent strong and statutory assurance that it will simply rein in the program. The prospect of expanding the program to subsidize broadband access raises serious concerns about potential huge cost increases. I would consider including broadband in the fund but, my colleagues, only if paired with reform that will

constrain growth in the fund at a minimum and preferably shrink it. I mean, that is the whole purpose of what we are trying to do. Thus, cost-containment reforms must be part of the mix.

I am encouraged that the bill requires the FCC to determine support for wireless carriers through a competitive bidding mechanism, and that is an important cost-cutting reform. Such a mechanism should also be applied to wireline providers. I also support provisions in the bill that require the FCC to act on needed reforms in other area, such as intercarrier compensation and traffic pumping.

I am still concerned about a couple of things. We need to target the money to the places and the people who really need it. The bill requires the FCC to establish a cost model that sets subsidy levels rather than using a market-based mechanism to subsidize a single wireline carrier in areas otherwise uneconomic to serve. Only wireless carriers would be subject to competitive bidding, and up to two wireless carriers could be subsidized in an area in addition to the incumbent wireline providers.

Carriers would also be allowed to continue under rate-of-return regulation. Although the FCC would not be allowed to “unreasonably increase,” end quote, the amount consumers pay, the contribution factor could still rise, and the fund would not be capped.

So, Mr. Chairman, I appreciate you holding this hearing. It is important to reexamine the goals and assess the results of the current program. We all agree that the system needs reform, and I hope we are able to work together towards a solution that is fair to all consumers.

Mr. BOUCHER. Thank you very much, Mr. Stearns.

The chairman of our full Energy and Commerce Committee, the gentleman from California, Mr. Waxman, is recognized for 5 minutes.

OPENING STATEMENT OF HON. HENRY A. WAXMAN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Mr. WAXMAN. I would like to begin my comments today by commending Chairman Boucher and Representative Terry for their efforts to bring forward legislation designed to reform the Universal Service High-Cost Fund. Chairman Boucher, in particular, has shown amazing leadership. We would not be here today without his dedication to universal service and his legislative acumen.

As the FCC’s National Broadband Plan recognized, broadband is a foundation for economic growth, job creation, global competitiveness, and a better way of life. It is one of the great infrastructure opportunities for the 21st century.

The universal service program represents our Nation’s historic commitment to ensure that all Americans have access to communications services, which has been a cornerstone of communications policy since the invention of the telephone. Before the adoption of the 1996 Telecommunications Act, this program was supported through a system of implicit subsidies designed to make phone service affordable in rural America. Some customers paid higher rates so that others could pay affordable rates.

The Telecommunications Act of 1996 turned that implicit subsidy into an explicit system that supports affordable phone service in rural America as well as communications services to schools, libraries, and rural hospitals. The Telecom Act also codified the FCC Lifeline and Link-Up programs that ensure low-income Americans, regardless of geography, have access to essential communications services, an issue championed by Representative Doris Matsui.

The challenge now, as the National Broadband Plan outlines, is to transform this program from one that supports telephone service to one that ensures that all Americans have access to broadband and to ensure that consumer contributions to the fund are being used for the intended purposes.

The draft legislation takes several positive steps. First, the draft legislation better targets subsidies to the areas that most need them in three key respects: first, calculating the necessary subsidy on a more precise, granular basis than the one used today; second, eliminating subsidies in those areas where competition has demonstrated that service can be provided without a subsidy; and, third, considering all the revenues that a provider earns using the subsidized facility instead of just a portion of that revenue.

The draft legislation also proposes a way to reduce the duplicative subsidies sometimes given to wireless providers by limiting the number of wireless carriers that are eligible for support.

In addition, the draft legislation gives the FCC the ability to change the contribution mechanism to better reflect the realities of the communications marketplace. As stakeholders know, the distinctions between interstate and intrastate have been blurred to the point that they are irrelevant. Contributions to the USF must reflect that reality.

There are areas where I have some questions, which I hope this hearing will help clarify. A key point of reform should be to make the system more efficient and save consumers money. I hope this hearing will help us understand how the savings and costs add up under the legislation.

Another key objective of reform is to provide a broadband service to all Americans. There are broad waiver provisions in this bill. We need to examine those provisions and their impact on the goal of universal broadband coverage.

In closing, I again want to thank the chairman and Representative Terry for their efforts. I look forward to working with them and other members of the committee as we move forward in this area.

Thank you, Mr. Chairman.

[The prepared statement of Mr. Waxman follows:]

HENRY A. WAXMAN, CALIFORNIA
CHAIRMAN

JOE BARTON, TEXAS
RANKING MEMBER

ONE HUNDRED ELEVENTH CONGRESS
Congress of the United States
House of Representatives
COMMITTEE ON ENERGY AND COMMERCE
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Majority (2021 225-2927
Minority (2021 225-3641)

Statement of Rep. Henry A. Waxman
Chairman, Committee on Energy and Commerce
Legislative Hearing on H.R. 5828, the Universal Service Reform Act of 2010
Subcommittee on Communications, Technology, and the Internet
September 16, 2010

I would like to begin today by commending Chairman Boucher and Representative Terry for their efforts to bring forward legislation designed to reform the Universal Service High Cost Fund. Chairman Boucher, in particular, has shown amazing leadership. We would not be here today without his dedication to universal service and his legislative acumen.

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The draft legislation takes several positive steps. First, the draft legislation better targets subsidies to the areas that most need them in three key respects:

First, calculating the necessary subsidy on a more precise, granular basis than the one used today;

Second, eliminating subsidies in those areas where competition has demonstrated that service can be provided without a subsidy; and

Third, considering all the revenues that a provider earns using the subsidized facility, instead of just a portion of that revenue.

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In addition, the draft legislation gives the FCC the ability to change the contribution mechanism to better reflect the realities of the communications marketplace. As stakeholders know, the distinctions between interstate and intrastate have been blurred to the point that they are irrelevant. Contributions to USF must reflect that reality.

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In closing, I again want to thank the Chairman and Representative Terry for their efforts. I look forward to working with you and other members of the Committee as we move forward in this area.

Mr. BOUCHER. Well, thank you very much, Chairman Waxman. And thank you for you and your staff participating so actively with us on this measure and offering very highly constructive recommendations, most of which we are seeking to reflect in this measure and believe we have embodied here.

The gentleman from Nebraska, Mr. Terry, who I have partnered with on a bipartisan basis now for several years to bring this measure forward, is recognized for 2 minutes.

OPENING STATEMENT OF HON. LEE TERRY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF NEBRASKA

Mr. TERRY. Thank you, Mr. Chairman. I appreciate working with you and our esteemed witnesses here.

This bill is about three C's: compromise, certainty, and cost savings.

To say this bill is a product of compromise might be the understatement of the year. We have worked for years, soliciting everyone's input, including those from the committee as well as the industry. As one might imagine, not everyone sitting here today totally agrees on what the best fix is, but we have reached a delicate balance here where we have buy-in from almost every entity in the industry and from the committee. Our success in finding a compromise is personified in the long list of companies and trade organizations that have endorsed this bill.

And, Mr. Chairman, if I can ask unanimous consent to add one more to the list, a letter from the American Farm Bureau Federation.

Mr. BOUCHER. Without objection.

[The information appears at the conclusion of the hearing.]

Mr. TERRY. "Certainty," you hear that word a lot when I was home over the break from our small-business owners. Well, if you are a small telecom business, you want the same thing, especially if you are in a high-cost area in rural America. You want to know that the Universal Service Fund is going to be fixed and you can rely on it in the future.

And now they will have the reassurance that the USF is reformed, it is efficient and able to continue to meet its goal that all should have access to the services at reasonable and comparable prices to those in suburban and urban areas. They no longer have to worry or wonder what might happen if the contribution factor continues to escalate. They will now have explicit support for their investments in broadband. Now they will have certainty.

Lastly, we are taking the much-needed step of reforming the USF to produce cost savings. For a number of reasons, the fund has grown quickly within the last few years and has become unsustainable. We recognize this and address it by putting into place a number of cost-saving measures that will not only stabilize the fund but also reduce its size.

Chairman Waxman outlined just a few of those cost-saving measures. Specifically, our bill implements a competitive bidding process for wireless carriers and eliminates USF support for wireline providers in competitive areas, while also ensuring that the contribution factor does not increase. In addition, the legislation finally di-

rects the FCC to fix their intercarrier compensation system and fix phantom traffic.

I would like to again thank our witnesses for being here today—it is an impressive panel—and their willingness to compromise. We have together produced a bill that will not only create cost savings but will provide much-needed certainty for those investing in today's telecommunications infrastructure. And I am proud to have worked with Chairman Boucher in this process and look forward to next week and the weeks coming on this bill.

Thank you, and I yield back.

Mr. BOUCHER. Thank you very much, Mr. Terry.

The gentleman from Pennsylvania, Mr. Doyle, is recognized for 2 minutes.

OPENING STATEMENT OF HON. MICHAEL F. DOYLE, A REPRESENTATIVE IN CONGRESS FROM THE COMMONWEALTH OF PENNSYLVANIA

Mr. DOYLE. Thank you, Mr. Chairman, for holding this hearing today on your bill to reform the Universal Service Fund.

For Members of Congress on both sides of the aisle and both chambers, from mayors of towns without broadband, to consumers who are paying billions of dollars per year so that their friends and loved ones in rural areas can get connected, I think everybody agrees that the fund is broken.

Your bill was an interesting approach to fixing it that I think merits thoughtful deliberation. I have a few technical questions on some topics, including traffic stimulation and implementation of the requirement that companies receiving Federal funding from the Universal Service Fund actually provide broadband. And I look forward to getting them answered today.

And, with that, Mr. Chairman, I will yield back.

Mr. BOUCHER. Well, thank you very much, Mr. Doyle.

The gentlelady from Tennessee, Mrs. Blackburn, is recognized for 2 minutes.

OPENING STATEMENT OF HON. MARSHA BLACKBURN, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF TENNESSEE

Mrs. BLACKBURN. Thank you, Mr. Chairman.

I want to welcome all of our witnesses that are here.

And, Mr. Chairman, you mentioned that there has been some revisions and some give and take. And I applaud you, Ranking Member Stearns, and the staffs for all the work on this.

I am encouraged by many of the proposals and reforms that are in this bill. Among those, I think that intercarrier compensation, the reforms there, that is important. I am pleased that the legislation takes a hard stance on traffic pumping. And it is long overdue that we introduce competitive bidding to the wireless industry.

However, there are still some places that we are needing to do some work. As I have stated over and over again in this subcommittee, it is difficult for me to look at the USF and not see a typical regressive D.C. tax. It keeps getting bigger, and I am extremely disappointed that the bill does not put a cap on the fund or put a limit on how big it should be. We are talking about a de-

clining-cost industry, where both technology and fiber are reducing their cost over time. So I would argue that the cost of support and maintenance of those services through the USF should also be declining, as well.

And I am hopeful that today's hearing can help re-center some discussion on this issue and move forward to finding a completion and a bill that can go to the floor.

I thank you. I yield back.

Mr. BOUCHER. Thank you very much, Mrs. Blackburn.

The gentlelady from California, Ms. Matsui, is recognized for 2 minutes.

OPENING STATEMENT OF HON. DORIS O. MATSUI, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Ms. MATSUI. Thank you, Mr. Chairman. And thank you for calling today's hearing. I would like to commend you for your leadership on efforts to reform the Universal Service Fund.

I would also like to welcome our witnesses.

Unfortunately, millions of Americans, particularly those in tough economic times, simply cannot afford the costs associated with in-home broadband service. As a result, they are at a competitive disadvantage when it comes to employment, education, and other opportunities. So we are seeing more and more disabled Americans, seniors, and teenagers traveling several miles to their nearest community center or library just to get online.

We know that broadband adoption rates are largely associated with income levels, and the cost of broadband services continues to be a barrier for hardworking families. According to the FCC, 28 million Americans do not subscribe purely because of affordability barriers.

That is why, just about 1 year ago today, I introduced H.R. 3646, the "Broadband Affordability Act," which would expand the Universal Service Fund's Lifeline Assistance Program for universal broadband adoption.

This proposal will ensure that all Americans living in urban and rural areas have access to affordable broadband services. We never know where the next great idea or invention will come, so we must continue to eliminate barriers to accessing broadband services for our constituents.

And I strongly believe that any reform to the Universal Service Fund needs to address broadband affordability barriers. I look forward to continue working with Chairmen Boucher, Waxman, and my colleagues on reforming the Universal Service Fund, and yield back the remainder of my time.

Mr. BOUCHER. Thank you very much, Ms. Matsui.

The gentleman from Ohio, Mr. Latta, is recognized for 2 minutes.

OPENING STATEMENT OF HON. ROBERT E. LATTA, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF OHIO

Mr. LATTA. Thank you, Mr. Chairman, Ranking Member Stearns. Thank you very much for holding this hearing today on H.R. 5828.

I applaud the chairman and Mr. Terry for working on this legislation that addresses reform of the Universal Service Fund. There

seems to be a consensus among stakeholders that action is needed, not only to ensure the feasibility and stability of the USF, but also to address the numerous issues surrounding its role in a changing marketplace.

There is no doubt, since the USF began, it has assisted numerous rural areas of this country to have access to telecommunication services. As we have discussed in previous hearings on the National Broadband Plan with the goal of reaching the remaining 5 percent of those who do not have access to broadband, there is an opportunity for the USF to be used to reach these remaining areas. Representing Ohio's largest agricultural district, I am keenly aware of the importance broadband deployment plays in economic development and the nexus this access has to job creation.

If the USF is expanded to include broadband services, I believe this should be done through the existing programs, not by creating a new funding stream or adding additional funding. It is my understanding that, in 1998, the total commitments to the fund totalled \$3.56 billion and, in 2009, that amount grew to over \$7.7 billion. This is tremendous growth over the past 10 years, and I have serious concerns that the funding will increase since the legislation there—there is not currently a cap on the fund or anything to ensure that the savings are offset. A cap will prevent uncontrolled growth as well as bring stability to the USF.

In addition to the concern about uncontrolled growth, there have been reports of fraud, waste, and abuse of the USF, especially in the E-Rate Program. I am pleased that this legislation establishes performance measures and audits of the USF to help ensure that fraud, waste, and abuse are not occurring in any of the USF programs.

I am hopeful that the interested stakeholder groups will continue to work on this legislation and address the issues surrounding the USF. And I believe that the positive benefits to the rural districts like mine have access for telecommunication services.

Again, I am opposed to an expansion of the government program that already has had increasing costs to consumers. It is my hope that the USF can be reformed without an increased cost to consumers directly or through the Federal Government's budget.

And thank you, Mr. Chairman. I yield back.

[The prepared statement of Mr. Latta follows:]

Congressman Robert E. Latta - The Committee on Energy & Commerce
Subcommittee on Communications, Technology & the Internet
Legislative Hearing on H.R. 5828, "Universal Service Reform Act of 2010"
Opening Statement – For the Record
September 16, 2010

MR. CHAIRMAN; RANKING MEMBER STEARNS: Thank you for holding this hearing on H.R. 5828. I applaud Mr. Boucher and Mr. Terry for working on legislation that addresses reform for the Universal Service Fund. There seems to be consensus among stakeholders that action is needed not only to ensure the feasibility and stability of the USF, but also to address the numerous issues surrounding its role in a changing marketplace.

There is no doubt that since the USF began it has assisted numerous rural areas of the country have access to telecommunications services. As we have discussed in previous hearings on the National Broadband Plan (NBP), with a goal of reaching the remaining 5% of those that do not have access to broadband, there is an opportunity for the USF to be used to reach these remaining areas. Representing Ohio's largest agricultural, I am keenly aware of the importance broadband

deployment plays in economic development and the nexus this access has to job creation.

If the USF is expanded to include broadband services, I believe this should be done through the existing program and not by creating a new funding stream, or adding additional funding. It is my understanding that in 1998 the total commitments to the fund totaled \$3.56 billion; in 2009, that amount grew to over \$7.7 billion. This is tremendous growth over the past ten years, and I have serious concerns that the funding will increase since in the legislation there is not currently a cap on the fund or anything to ensure that the savings are offset. A cap will prevent uncontrolled growth as well as bring stability to the USF. In addition to the concern about uncontrolled growth, there have been reports of fraud, waste and abuse of the USF, especially in the e-Rate program. I am pleased that the legislation establishes performance measures and audits of the USF to help ensure that fraud, waste and abuse are not occurring in any of the USF programs.

I am hopeful that the interested stakeholder groups will continue to work on this legislation to address the issues surrounding the USF. I

believe there are positive benefits to rural districts like mine for access to telecommunications services. However, I am opposed to an expansion of a government program that already has had increasing costs to consumers. It is my hope that the USF can be reformed without an increased cost to consumers directly, or through the federal government's budget.

Thank you. [Yield Back]

Mr. BOUCHER. Thank you, Mr. Latta.

The gentleman from California, Mr. McNerney, is recognized for 2 minutes.

OPENING STATEMENT OF HON. JERRY MCNERNEY, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF CALIFORNIA

Mr. MCNERNEY. Thank you, Mr. Chairman, for convening today's hearing to discuss the Universal Service Reform Act. It is good to see progress being made on this issue.

The universal service program was created over 10 years ago. Well, that may not seem long in many contexts, but in telecommunications that is an eternity. With so many advances in our technology, such as the rapid expansions of Internet and cell phones, it is now a good time to reassess our current policy and make appropriate updates.

I commend the chairman and Representative Terry for their bipartisan work and taking into consideration important issues such as ensuring broadband service to those who currently may not be adequately served.

As we hear from today's witnesses, I hope to learn how we can continue to improve the bill and prevent any unintended negative consequences. We all want to develop legislation that benefits consumers and allows businesses to compete and thrive, and I look forward to working with my colleagues to craft the best possible legislation.

Thank you, Mr. Chairman. And I yield back the balance of my time.

Mr. BOUCHER. Thank you, Mr. McNerney.

The gentleman from Washington State, Mr. Inslee, is recognized for 2 minutes.

Mr. INSLEE. Thank you.

I just want to point out that we have a real need, connecting the talent in our tribal communities. And I am hopeful that, as this bill proceeds, we will find a way to get some tribal representation on the board making decisions here. I look forward to making sure we get that done.

Thank you.

Mr. BOUCHER. Thank you, Mr. Inslee.

The gentlelady from Florida, Ms. Castor, is recognized for 2 minutes.

OPENING STATEMENT OF HON. KATHY CASTOR, A REPRESENTATIVE IN CONGRESS FROM THE STATE OF FLORIDA

Ms. CASTOR. Thank you, Mr. Chairman.

And thank you to the witnesses for being here today.

Universal service reform is an issue I have been concerned about for some time. I am a cosponsor of H.R. 3646, the "Broadband Affordability Act," introduced by my colleague, Representative Matsui, which would reduce the cost of broadband services for low-income urban and rural customers along the lines of the Lifeline and Link-Up programs within the USF.

Lifeline and Link-Up have helped thousands of families afford the cost of telephone service since the mid-1980s, but now it is cell

phones and the Internet that have become the indispensable tools in our daily lives. Many of us take them for granted, but there are others in our communities who can't even afford the most basic services. So I am glad to see that the bill before us today gives the FCC the authority to include broadband within the USF.

There is an assumption that urban areas have plenty of access to broadband, but there are significant gaps. For many, broadband is out of reach. But it doesn't have to be that way. Expanding the Lifeline and Link-Up program discounts would lower the cost of broadband for families living on the margins.

We also must address the severe inequity in the USF. I have pointed out before, Floridians far overpay into the USF without receiving some sort of equitable return. The new cost model put forward by the FCC must correct this inequity as we implement the National Broadband Plan and reform the Universal Service Fund.

Thank you very much. And I yield back.

Mr. BOUCHER. Thank you, Ms. Castor.

The gentleman from Connecticut, Mr. Murphy, is recognized for 2 minutes.

Mr. MURPHY. Thank you, Mr. Chairman. I look forward to hearing from the witnesses, and I will waive an opening statement.

Mr. BOUCHER. Thank you, Mr. Murphy. We will add 2 minutes to your questioning time.

The gentlelady from the Virgin Islands, Mrs. Christensen, is recognized for 2 minutes.

Mrs. CHRISTENSEN. Thank you, Mr. Chairman. I, too, would just like to welcome the witnesses and waive my opening statement.

Mr. BOUCHER. Thank you, Mrs. Christensen. Two minutes to you also.

That concludes opening statements by members of the subcommittee.

I am pleased now to recognize and introduce briefly our panel of witnesses. And we want to thank each of you for joining us here today.

Carol Matthey is the deputy bureau chief of the Wireline Competition Bureau at the Federal Communications Commission.

Walter McCormick is president and chief executive officer of the United States Telecom Association.

Shirley Bloomfield is chief executive officer of the National Telecommunications Cooperative Association, NTCA, and is testifying today on behalf of NTCA, OPATSCO, and the Western Telecommunications Alliance, all associations of rural carriers.

Steve Davis is the senior vice president for public policy and government relations at Qwest Corporation.

Kathleen Grillo is the senior vice president for Verizon.

And James Assey is executive vice president of the National Cable and Telecommunications Association.

We welcome each of you. And, without objection, your prepared written statements will be made part of our record. We would welcome your oral summaries and ask that you keep those to approximately 5 minutes.

Ms. Matthey, we will be happy to begin with you.

STATEMENTS OF CAROL MATTEY, DEPUTY BUREAU CHIEF, WIRELINE COMPETITION BUREAU, FEDERAL COMMUNICATIONS COMMISSION; WALTER MCCORMICK, PRESIDENT AND CHIEF EXECUTIVE OFFICER, UNITED STATES TELECOM ASSOCIATION; SHIRLEY BLOOMFIELD, CHIEF EXECUTIVE OFFICER, NATIONAL TELECOMMUNICATIONS COOPERATIVE ASSOCIATION, NTCA; STEVEN DAVIS, SENIOR VICE PRESIDENT FOR PUBLIC POLICY AND GOVERNMENT RELATIONS, QWEST CORPORATION; KATHLEEN GRILLO, SENIOR VICE PRESIDENT, VERIZON; JAMES ASSEY, EXECUTIVE VICE PRESIDENT, NATIONAL CABLE AND TELECOMMUNICATIONS ASSOCIATION

STATEMENT OF CAROL MATTEY

Ms. MATTEY. Thank you, Chairman Boucher, Ranking Member Stearns, members of the subcommittee. Thank you for the opportunity to testify today about the "Universal Service Reform Act of 2010."

Universal service historically has been a significant success story in the United States. In addition to incentivizing the private sector to bring affordable voice service to virtually all reaches of the country, the existing program has played an important role in strengthening communities and our economy by supporting modern networks capable of delivering broadband as well as voice service to many rural Americans.

But the current system, which wasn't designed to explicitly support broadband, is not working for everyone. While consumers in some places in rural America have access to some of the best broadband networks in the country, others don't have access to broadband at all. While many speak of an urban-rural divide for broadband service, the more troubling trend is a rural-rural divide. Under the existing universal service rules, not all providers have the same incentives to upgrade their networks to provide broadband, and some have economic incentives to invest in areas already served by unsubsidized competitors.

Maintaining the status quo is unlikely to achieve affordable and universal access to broadband. Critical elements of the current system, such as how we collect the money to support universal service and the intercarrier compensation framework, must be reexamined in light of changes in technology platforms and market dynamics, changes that the Universal Service Reform Act expressly contemplates.

The Commission shares the goals expressed by Chairman Boucher and Representative Terry when they highlighted the need for comprehensive and forward-looking reform that will ensure that sufficient universal service support is available on a technology-neutral basis.

In March of this year, the Commission unanimously adopted a joint statement on broadband, calling for the system to be comprehensively reformed to increase accountability and efficiency and encourage targeted investment in broadband infrastructure. I would like to elaborate briefly on a few shared principles that underlie the bill and the FCC's current efforts.

First, forward-looking policies are critical. Simply because we have done things a certain way in the past does not mean those same policies make sense in a broadband world. It is incumbent upon all of us to take a close look at the current system to determine how to move forward towards our goal of advancing broadband. We need to find a foundation of continued private-sector investment and a pathway for broadband to evolve in the future. Our rules must be based on the technology and economic realities of today and tomorrow, not the last century.

Second, targeted, technology-neutral, and sufficient levels of support are essential. We should target support only to those areas that really need it. We need to provide sufficient support to establish an effective public-private partnership in which support is made available in exchange for a commitment to meet reasonable public interest obligations.

Third, a revamped program requires oversight and accountability. The bill's vision and ours is to ensure USF dollars are spent in a responsible way. This means maintaining effective oversight. Whoever receives funding should be accountable for building out, and we should ensure that USF benefits as many unserved and underserved Americans as possible with no more support than is truly necessary.

Fourth, we should remember that universal service is fundamentally about consumers in all parts of the country. Ultimately, it is the consumer that pays for universal service. As we go through this process of making policy choices and compromises, we should never lose sight of the burden and benefits to consumers.

Finally, we must move quickly but wisely. Market participants need clarity and regulatory predictability so that they can make informed business decisions. We hope that all stakeholders will actively and constructively engage so that we can move swiftly to establish clear and sensible policies for the future.

To conclude, on a personal note, as a member of the Commission staff who has worked on universal service issues since 2000, I am very encouraged by the bipartisan consensus and recognition of the need for reform. We at the FCC appreciate the leadership of the chairman and Representative Terry in introducing this bill. And we look forward to working with the subcommittee and others to ensure that reform moves forward.

Thank you again for the opportunity to testify, and I will be happy to answer any questions.

[The prepared statement of Ms. Matthey follows:]

**Written Statement of
Carol Matthey
Deputy Chief, Wireline Competition Bureau
Federal Communications Commission**

Hearing on H.R. 5828, "Universal Service Reform Act of 2010"

**Subcommittee on Communications, Technology, and the Internet
United States House of Representatives
September 16, 2010**

Chairman Boucher, Ranking Member Stearns, Members of the Subcommittee, thank you for the opportunity to testify today about the important subject of universal service and H.R. 5828, the Universal Service Reform Act of 2010.

Following the introduction of H.R. 5828, Representative Terry stated that the bill's goal is to ensure "everyone in America is connected into the 21st century telecommunications world." That objective is broadly shared by the FCC as we undertake the process of considering the recommendations included in the National Broadband Plan submitted to Congress in March.

The National Broadband Plan recognized the important role that the private sector has played and must continue to play in investing in broadband facilities as well as promoting investment and innovation in broadband technologies and services. But, as Chairman Boucher and Representative Terry noted when introducing H.R. 5828, some Americans live in areas for which there simply is not an economic case for any provider to build, upgrade and maintain vital communications infrastructure. That is why we have what is known as the high cost program in the Universal Service Fund.

Universal service historically has been a significant success story in the United States. In addition to incenting the private sector to bring affordable voice service to virtually all reaches of the country, the existing high cost program has played an important role in strengthening communities and our economy by supporting modern networks capable of delivering broadband

as well as voice services to millions of rural Americans who would not otherwise have such access. For example, the National Exchange Carriers' Association reported that a sampling of small telephone companies made approximately \$5 billion of gross investments, mostly to modernize their networks, between 2006 and 2009.

But, as I'm sure many of your constituents tell you, **the current system**, which wasn't designed to explicitly support broadband, **is not working for everyone**. While consumers in some places in rural America have access to some of the best broadband networks in the country, others don't have access to broadband at all, even though they are served by providers eligible for universal service support. While many speak of an urban/rural divide for broadband service, the more troubling trend is a rural/rural divide that reflects the antiquated structure and incentives of our current high cost program.

Under the existing universal service rules, not all providers have the same incentives to upgrade their networks to provide broadband; some only receive sufficient support to maintain existing voice service. And some of those providers that are able to build broadband networks through universal service support have limited accountability for where the money is used and have economic incentives to invest most heavily in areas that are already served by unsubsidized competitors.

Rules originally designed for a circuit-switched, voice network no longer make sense as we shift to packet-switched, broadband networks capable of supporting countless applications, including voice. While we have largely achieved the goal of universal voice service, maintaining the status quo policy framework is unlikely to achieve the goal of affordable and universal access to broadband. Critical elements of the current system such as how we collect the money to support universal service and the intercarrier compensation framework must be re-examined in

light of changes in technology platforms and market dynamics – something that the Universal Service Reform Act of 2010 expressly contemplates. These issues are all inter-related.

The Commission shares the goals expressed by Chairman Boucher and Representative Terry when they highlighted the need for “comprehensive and forward-looking” reform that will “ensure that sufficient universal service support is available on a technology-neutral basis.” In fact, the Commission has unanimously adopted a “Joint Statement on Broadband” calling for the Universal Service Fund and the intercarrier compensation system to be “comprehensively reformed to increase accountability and efficiency, encourage targeted investment in broadband infrastructure, and emphasize the importance of broadband to the future of these programs.”

I would like to elaborate on a few of these shared principles that underlie the Universal Service Reform Act and the FCC’s current efforts:

Forward-looking policies are critical because networks and technology are changing. The marketplace is changing. The opportunities and challenges are changing. Our policies must anticipate these changes. Simply because we have done things a certain way in the past does not mean those same policies and structures make sense in a broadband world. It is incumbent upon all of us to take a close look at the current universal service system to determine how to move toward our goal of advancing broadband. We need to provide a foundation for continued private sector investment in broadband and a pathway for broadband to grow and evolve in the future. Our rules must be forward looking, technology neutral, and incent judicious investment – based on technology and economic realities of today and tomorrow, not the last century.

Targeted, technology-neutral and sufficient levels of support are essential to incentivize private sector entities to invest in partnership with the public sector. We should

be looking at ways to target support only to those areas that really need it to deploy and sustain broadband networks capable of providing high-quality broadband and voice services. We need to provide sufficient support to meet the mandates that come with that support, and recognize that expectations have to match economic reality. And we should do so without interfering with innovation and private investment in areas that can sustain unsubsidized service.

Responsible reform requires an effective public/private partnership in which support is made available in exchange for a commitment from providers to meet reasonable public interest obligations. We look forward to working with all the stakeholders – including state, local and Tribal governments, as well as service providers, community and consumer groups – to develop a unified vision of the obligations that we expect recipients of universal service funding to meet in the 21st century.

A revamped program also requires **oversight and accountability**. The bill's vision, and ours, is one in which the government sets forth explicit goals for the program and clear expectations for participants, and then takes active steps to ensure that USF dollars are spent in a responsible way that meets those goals and expectations. This means maintaining effective oversight of the system to ensure that those who receive support are responsible stewards of the money they are receiving from the American public. Whoever receives the funding should be held accountable for building out and serving consumers, and we should ensure that USF benefits as many unserved and underserved Americans as possible with no more public support than is truly necessary.

As we move forward, we should remember that **universal service is fundamentally about consumers in all parts of the country**. Ultimately, it is the consumer who pays for universal service, and all consumers, whether they live in rural or urban areas, benefit from

additional Americans connecting to the network. Ensuring access to quality, affordable services at reasonably comparable rates for all consumers is not easy, but that is the goal set forth in the Telecommunications Act of 1996. That is the fundamental premise upon which our universal service policy has been based, and that will continue to guide our FCC efforts going forward as communications evolve in the future.

Achieving this goal will involve choices and compromises because of the inherent tension between increasing the contribution burden on consumers and providing support where needed. But as we go through the process of making policy choices and compromises, we should never lose sight of the burden and benefits to consumers. Indeed, if the burden on consumers becomes too high, it could undermine the national consensus that universal service is a shared responsibility for all.

And, finally, **we must move forward with the process quickly, but wisely.** Market participants need **clarity** and **regulatory predictability** so they can make **informed business decisions**, and have time to implement changes necessary to adapt to any new frameworks. Although many difficult and complex issues lie ahead, these complexities are not insurmountable if all parties are willing to work together to achieve universal broadband service for American consumers. It is in everyone's interest to know the rules of the road as quickly as possible, even though there may be a period of extended transition once new rules are adopted. We hope that all stakeholders will engage actively and constructively throughout this process of reform so that we can move swiftly to establish clear and sensible policies for the future.

On a personal note, as a member of the Commission staff who has been working on universal service issues since 2000, I am encouraged by the bipartisan consensus and the recognition of the need for reform. No one would suggest that USF and ICC reform is a simple

process. Change never is. But we all agree that reform is necessary to make broadband the technology of choice for Americans in the 21st century in a global economy, and that success depends on all stakeholders working together towards a shared end goal. We at the FCC appreciate the leadership of Chairman Boucher and Representative Terry in introducing H.R. 5828, and we look forward to working with all of the members of the Subcommittee and other stakeholders to ensure that reform moves forward.

Thank you again for the opportunity to testify this morning. I will be happy to answer any questions you may have.

Mr. BOUCHER. Thank you very much, Ms. Matthey. We are delighted to have you here.

Mr. McCormick?

STATEMENT OF WALTER MCCORMICK

Mr. MCCORMICK. Mr. Chairman, Ranking Member Stearns, Mr. Terry, and members of the subcommittee, thank you for the opportunity to testify today in support of this important legislation.

It is hard to overestimate the importance of broadband to our Nation's economy, to America's competitiveness, to education, to health care, to environmental sustainability, to job creation, and to our citizens' quality of life. Today broadband has been built out to about every place in America where a reasonable business case can be made for deployment. Over the course of the last decade, broadband service providers have invested over \$700 billion in deploying broadband infrastructure.

According to the FCC's National Broadband Plan, fixed broadband service of 4 megabits or more is now available to 95 percent of our population. This is an extraordinary accomplishment. Consider that earlier this year Congress passed universal health care that, when fully implemented some years from now, aims to cover 95 percent of Americans. We are there today with broadband.

But getting to the last 5 percent of Americans, it is expensive. The FCC estimates that it is going to cost about \$24 billion. It can only be done if Congress and the FCC address the financial fundamentals that lie at the foundation of rural service, which are universal service and intercarrier compensation. This bill does that.

We are grateful to you, Mr. Chairman, and to Mr. Terry for the thought that you put into this legislation, for the attention to detail, for the inclusive process that you employed, and for the consensus that you forged.

This bill addresses each of the key issues that are central to the integrity of universal service going forward. It expands the contribution base to include new technologies. It reforms USF distributions to target support where it is most needed, to reduce duplication, to balance competing interests, and to focus on broadband. It mandates reform of intercarrier compensation, the means by which carriers receive payment for the use of their networks. It addresses the egregious abuses of the system that have arisen with regard to phantom traffic and traffic pumping. It reforms the audit process. It prevents the Commission from restricting high-cost support to primary lines. And it resolves the longstanding administrative problem associated with the Anti-Deficiency Act.

So we endorse this bill. We do so cognizant of the fact that our industry did not get everything that it wanted. But we do so in the spirit of compromise, in the spirit of bipartisanship that characterizes this package, and with the recognition that it would be imprudent to let the perfect be the enemy of the good, both for our industry and for our Nation.

This bill deals with complex matters. It allocates large sums of money, and it impacts a variety of competing interests. The balance that has been struck is a fair but very delicate one, and it could tip easily. We recognize that to pull at one thread is to unravel the

fabric of an impressive blueprint for investment in 21st-century broadband communications.

So, Mr. Chairman, based upon the substance of this package, coupled with clear assurances and a legislative history that assure our industry that it will not result in unfunded mandates, and this committee's commitment to close oversight of Commission implementation, we recommend its passage.

Again, thank you for your extraordinary work on this very important issue.

[The prepared statement of Mr. McCormick follows:]

**Testimony of
Walter B. McCormick, Jr.
President and CEO, United States Telecom Association
before the
House Committee on Energy and Commerce
Subcommittee on Communications, Technology and the Internet
“The Universal Service Reform Act of 2010” (H.R. 5828)
September 16, 2010**

Chairman Boucher, Ranking Member Stearns, and Members of the Subcommittee:

Thank you for the opportunity to appear before you today to discuss updating the laws, and in turn securing the financial fundamentals, underlying the provision of universal service to rural Americans. I am Walter McCormick, President and CEO of the USTelecom Association. USTelecom represents innovative broadband companies ranging from some of the smallest rural telecoms in the nation to some of the largest companies in the U.S. economy. Our members offer a wide range of advanced broadband services, including voice, internet access, video, and data, on both a fixed and mobile basis. What unites our diverse membership is our shared determination to deliver broadband services to all Americans – regardless of their location – a goal to which we know this Subcommittee is equally committed.

The universal service program is an American success story. Today phone service is as ubiquitous as electricity and clean water throughout our nation. However, new technologies arise and evolve, and so it is time for universal service and the related regulatory framework governing payments among carriers to be updated to reflect the seismic changes in communications that have occurred over the nearly 15 years since passage of the 1996 Telecom Act. Paramount among these changes is the way in which broadband connections to the Internet have joined voice service as an integral part of our lives.

Over the last decade, broadband providers have invested well over \$700 billion in building and upgrading broadband networks. Reflecting the challenges of serving our Nation’s vast geography and varied terrain, investment on a per capita basis by broadband providers in the U.S. far exceeds that of other countries to which we are often compared, such as Japan, South Korea, and the United Kingdom. Ensuring that all Americans can enjoy the benefits of robust broadband is a goal USTelecom strongly supports. And because of the massive private sector investment in building broadband networks, we are close to this goal. According to the FCC’s National Broadband Plan, robust broadband is available to 95% of the country. Getting to 100% will require an efficient and effective universal service program and sensible reform to the Federal Communications Commission’s (FCC) regulatory framework for payments between and among carriers.

Chairman Boucher and Representative Terry have thoughtfully crafted a bill that carefully balances many competing interests to modernize universal service and to bring

robust broadband to areas of rural America where today's business case would not support such deployment. In particular, H.R. 5828 provides for explicit support of broadband, better targets that support, and strives to match explicit support for the construction and operation of broadband networks with incentives to provide broadband service where it is not available. And by addressing intercarrier compensation as well as universal service, the bill takes a comprehensive approach to addressing the financial fundamentals that will help spur private investment in broadband facilities. We strongly support and share Chairman Boucher's and Representative Terry's commitment to providing all Americans an opportunity to have access to broadband, and at the same time we deeply appreciate their efforts to ensure that the legislation does not impose unfunded mandates on broadband providers as we work to attain that objective. For that reason, and because H.R. 5828 as introduced would bring essential reforms not only to the Universal Service Fund (USF) program but also to the current intercarrier compensation regime, USTelecom is proud to endorse this legislation.

While the intercarrier compensation provisions comprise a smaller portion of the legislation, the dollars involved are at least twice as much as currently available high-cost universal service support. Thus, the two systems must both be addressed because they are, by and large, opposite sides of the same coin. Universal service funds provide *explicit* subsidies to support reasonably priced services. By contrast, the fundamental problem with the existing intercarrier compensation system is that it is riddled with *implicit* subsidies that can no longer be maintained in today's era of new and competitive communications technologies. The transition from implicit to explicit support must be synchronized in a logical way that recognizes the investments telecommunications companies have made in reliance on existing mechanisms.

I will return to the subject of intercarrier compensation shortly, but please permit me first to note the important improvements the Boucher-Terry bill would make in the universal service program. Most importantly, the bill clarifies the FCC's authority to collect funds in a variety of ways to then distribute as universal service support. It authorizes methodologies including use of intrastate as well as interstate revenues, working telephone numbers used by communications providers, or any other current or new connections to the network. It properly broadens the base of contributors and provides the FCC with flexibility to use any or a combination of several methods to more fairly and equitably collect universal service funds.

We also appreciate the inclusion in the bill of provisions that address particular issues with the current system – the potential for disruption in the universal service program by application of the Anti-Deficiency Act and the inequities of restricting support to primary lines. Congress has addressed both over the years in annual appropriations legislation, but this bill would include those fixes in permanent law.

The bill strikes the proper balance between the need for universal service support for broadband while not unreasonably increasing the burden that falls on consumers to fund universal service. It obligates providers to build out broadband facilities to unserved areas, but also makes necessary changes to ensure financial support for meeting those obligations by, among other things, better targeting available funds. And it includes

essential relief to providers in situations in which the mandate and the available support cannot be appropriately matched.

Under today's system, rural consumers may be penalized by virtue of which company provides them service. The bill would eliminate that inequity by targeting rural areas for USF regardless of which company is providing service there and by eliminating the parent trap, which penalizes a rural carrier seeking to buy an exchange based solely on the seller's identity, rather than on the inherent characteristics of the area being served. That is the right and fair way to approach universal service support.

The Boucher-Terry bill also appears to appropriately balance competing interests, in its efforts to better target support by reducing or eliminating high-cost support provided in areas where 75 percent or more of the households have voice and broadband service available from another wired provider, typically a cable company. To ensure consumers are protected, cable companies would be subject to a set of obligations similar to those for incumbent telecommunication providers – such as the basic requirement to provide service to any customer requesting it in the company's service area. Support would then be targeted to the non-competitive areas that tend to have the highest costs. This mechanism, then, seeks to target funds to the truly high-cost areas and conserves scarce universal service funds.

Mr. Chairman, as you well know, it is not uncommon in the legislative process for one stakeholder or another to seek a tweak here or a change there that will make the legislation “just a little bit better” for them. But in this instance, we would respectfully caution that changes to this delicately balanced package potentially risk undermining the compromises you and Representative Terry have worked so hard to forge. The bill as introduced strikes a very careful balance between establishing obligations to provide service in even the most financially challenging areas and the funding available to support the construction and operation of broadband networks in those areas. Mandates that exceed the amount of support provided will not achieve their intended objective. Indeed, they risk driving broadband providers out of the program entirely. As this bill moves through the legislative process, it is very important that the delicate balance you have struck here not be upset by unrealistic expectations about what can or should be accomplished within the limits of the funding being made available.

Let me return now to the other subject of H.R. 5828, intercarrier compensation – the complex regulatory mechanism by which providers pay each other for carrying voice calls on each other's networks. The actual costs of terminating a call are the same no matter where the call originated. However, as a result of the implicit regulatory subsidies mentioned earlier, the rate for terminating a call may be vastly different depending on the origin of the call. Under this system, regulatory arbitrage has become a serious financial problem in the industry, creating an unnecessary obstacle to efficient network investment and operation. The FCC has been struggling with reforming its compensation rules for a decade without success. H.R. 5828 provides much needed guidance, clarifies certain jurisdictional issues, and sets a deadline for the FCC to complete comprehensive reform. The bill also provides guidance on two important elements of reform – traffic pumping and phantom traffic – that are long overdue for FCC action.

Traffic pumping is a scheme by which communications companies artificially generate huge volumes of calls, typically through the offering of services like free conference calling, and then bill other carriers at the highest possible compensation rate. These particular compensation rates were originally established to keep consumer charges reasonable in rural areas, where providers typically have high deployment costs but low average call volumes. Today these rates are being taken advantage of by entities using new technologies with very low deployment costs and tremendously high call volumes. These charges are ultimately borne by all consumers of long distance services. As the National Broadband Plan explained, “because the arbitrage opportunity exists, investment is directed to free conference calling and similar schemes for adult entertainment that ultimately cost consumers money, rather than to other, more productive endeavors.”

Phantom traffic is an even simpler and more pernicious arbitrage scheme – communications companies send traffic over the network to and through other companies, but don’t provide information sufficient for the traffic to be identified. As the National Broadband Plan explained, “traffic is masked to avoid paying the terminating carrier intercarrier compensation entirely, and/or redirected to make it appear that the call should be subject to a lower rate.” If you can’t identify the traffic, you can’t bill for it. So the costs of terminating phantom traffic are passed on to others. The legislation addresses phantom traffic by including a simple but important provision that requires any communications provider that originates traffic to sufficiently identify it.

As much as we appreciate and support the bill’s inclusion of provisions to end both these regulatory arbitrage schemes, we hasten to emphasize that the FCC has a more than sufficient record to deal with them right now. It has received extensive public comment on both traffic pumping and phantom traffic – indeed, USTelecom has provided the Commission with detailed proposals for addressing both these issues that have received broad support. Moreover, the National Broadband Plan urges the FCC to adopt rules to reduce these arbitrage opportunities. It is critical that the Commission not use the pendency of legislation to delay further in adopting fixes to these rapidly growing problems, which it has ample jurisdictional authority to address. And so in addition to moving forward with this legislation, we hope the Subcommittee will encourage the FCC to follow the common sense guidance in the bill and adopt rules immediately.

By squarely addressing the thorny issues of intercarrier compensation reform and universal service, the Universal Service Reform Act of 2010 represents an important milestone in the effort to establish a sound, modern regulatory framework for the future deployment and operation of broadband networks in rural America and throughout the Nation. Adoption of the key elements of the bill, whether legislatively or through speedy FCC action where appropriate, would remove a great deal of regulatory uncertainty and spur investment in broadband facilities. USTelecom looks forward to continuing to work with you, Chairman Boucher, as well as with you Representative Terry, and the members of the Subcommittee, to accomplish these worthy goals.

Mr. BOUCHER. And thank you for that excellent testimony.
Ms. Bloomfield?

STATEMENT OF SHIRLEY BLOOMFIELD

Ms. BLOOMFIELD. Thank you very much, Chairman Boucher, Ranking Member Stearns, Congressman Terry, members of the subcommittee. Good morning, and thank you very much for the invitation to testify today on H.R. 5828, the "Universal Service Reform Act of 2010," which we are also very much in support of.

NTCA, which represents more than 580 rural telephone companies, is who I am here on behalf of, along with my colleagues, OPATSCO and WTA. And, together, we represent 1,100 rural, rate-of-return regulated, community-based communications and broadband service providers from around the Nation. Collectively, our member companies serve about one-third of the landmass of this country but about 5 percent of the total subscriber lines.

So we would like to thank you very, very much for your leadership, Chairman Boucher and Congressman Terry, in particular, for your longstanding focus and understanding of both the critical importance of universal service support for today's communication networks and the need for reform to usher in a new era of advanced communications.

As you know, OPATSCO and WTA and NTCA have endorsed 5828. The bill represents a laudable effort to seek compromise between many different viewpoints and interests on these very important issues. Your ability to find some common ground on such a complex topic is a testament to your efforts to the American public and a dedication to advancing telecommunications policy to better reflect the needs of the communications broadband-focused world.

Universal service continues to be the cornerstone of our Nation's communications policy and ensures that Americans living all across the country, and particularly in rural areas, receive services that are comparable to those in performance and price to those living in urban areas. And it is an opportunity for everybody in this country to benefit from a nationwide, integrated, advanced communications network.

A typical self-sustaining business model that works in an urban area is much more difficult to achieve in a rural market. And those of you who have rural areas in your congressional districts know what I mean, when you are driving for miles, how difficult it is to put a telecommunications plant in those markets.

In those high-cost areas, universal service is critical to overcoming the economic challenges of deploying communications networks. So, as members of the industry and Members of Congress recognize, it is time to update the universal service program and to reflect the shift from voice to a broadband world.

The "Universal Service Reform Act of 2010" contains a number of program modifications that we support and that we think are very important and that I detail a little bit more further in my testimony, but I do want to hit on a couple of them.

The bill maintains rate-of-return regulation for eligible communication providers, ensuring the needed stability and predictability in cost recovery to promote investment in high-cost, low-density parts of our country. It defines universal service to include high-

speed broadband service so that the support for the deployment and operation of broadband networks will be explicit. It also requires a contribution to the Universal Service Fund from a wider range of providers, including all broadband providers. And it requires the FCC to act on intercarrier comp reform in the near term and to allow the USF growth factor to accommodate intercarrier comp flows directed to it.

So, although the bill contains these very important modifications to USF—our organizations do endorse the bill—we also have a couple of things that do raise some concerns for us: reducing or eliminating high-cost support in competitive areas and the implementation of a new, unproven cost model that may not permit rural providers to meet universal service goals of providing reasonable, comparable, and reliable service in high-cost areas.

We are hopeful that if this legislation is adopted we can work with all of you to define and implement these measures in a way that acknowledges the critical role that rural telecommunication providers continue to play as carriers of last resort in their community. We also hope that the Congress and the FCC, if they are to act and implement any provisions, will recognize the very unique nature of some of these rural markets.

Mr. Chairman, I want to thank you again for inviting me to be here with you. Your knowledge of the industry, your bipartisan efforts with Representative Terry, your commitment to strengthening and advancing communications for all Americans, both urban and rural, make us very fortunate to have you serving on this committee.

The bill that we are discussing here today is a product of many hard years of work, a lot of effort on behalf of a lot of people. And we look forward to continuing to work with you to improve this measure and to answering any questions that the committee may have.

Thank you very much.

[The prepared statement of Ms. Bloomfield follows:]



The Voice of Rural Telecommunications
www.ntca.org

Statement by

Shirley Bloomfield
Chief Executive Officer
National Telecommunications Cooperative Association

On behalf of the

NTCA
National Telecommunications Cooperative Association
OPASTCO
Organization for the Promotion and Advancement of Small Telecommunications Companies
WTA
Western Telecommunications Alliance

Before the

United States House of Representatives
Committee on Energy and Commerce's
Subcommittee on Communications, Technology, and the Internet

In the Matter of

H.R. 5828, The "Universal Service Reform Act of 2010"

September 16, 2010

Introduction

Chairman Boucher, Ranking Member Stearns, members of the Subcommittee, good morning and thank you for the invitation to participate in today's discussion regarding H.R. 5828, The Universal Service Reform Act of 2010, which is sponsored by Chairman Boucher and Rep. Terry.

I am the Chief Executive Officer of the National Telecommunications Cooperative Association (NTCA), which represents more than 580 small, rural telecommunications cooperatives and commercial companies. However, my remarks today are also being made on behalf of the Organization for the Promotion and Advancement of Small Telecommunications Companies (OPASTCO), and the Western Telecommunications Alliance (WTA), which along with NTCA, represent more than 1,100 rural rate-of-return regulated community-based communications and broadband service providers from around the nation. Collectively, the service territories of these companies cover more than one-third (37%) of the nation's land mass while their total subscriber base accounts for only about 5% of the national total.

Our organizations would like to thank the members of the Subcommittee – and Chairman Boucher and Rep. Terry, in particular – for their long-standing focus on and understanding of both the critical importance of universal service support for today's telecommunications networks, and the need for reform to usher in a new era of advanced communications. As you know, OPASTCO, NTCA, and WTA have endorsed H.R. 5828. The bill represents a laudable effort to seek compromise between many different viewpoints and interests on important issues. Your ability to find some common ground on such a complex and controversial topic is a testament to your efforts to serve the American public and your dedication to advancing telecommunications policy to reflect better the needs of a broadband-focused world.

Universal service continues to be a cornerstone of our nation's communications policy. It ensures that Americans living in rural areas of the country receive services comparable in

performance and price to those living in more urban areas. We must continue working to ensure that all Americans, including those living in rural areas, have the opportunity to experience the benefits offered by a nationwide integrated advanced communications network. Indeed, for consumers in rural or remote communities, broadband represents a vital link to the rest of the world for the most basic of communications, and it will play an even more important role in such areas as civic, economic, educational, and medical interactions increasingly migrate online.

The Universal Service Reform Act of 2010

Today, telecom providers and policy makers alike are shifting their primary focus from voice services to broadband, which offers the promise of being the great equalizer between rural and non-rural areas of our nation. Rural communications service providers are working to replicate the success of their telephone service build-out by steadily deploying broadband infrastructure and related services to an increasing percentage of their subscribers.

But this task is not easy, and more remains to be done. A typical self-sustaining business plan in an urban area is much more difficult to identify and implement in rural markets. It is in these high-cost areas that universal service remains critical to overcome the economic challenges of deploying communications networks. As members of the industry and Members of Congress recognize, it is time to update the universal service program to reflect this shift from voice to broadband. The Universal Service Reform Act of 2010 would support such a transition and would enable many other important steps to update and improve the program.

The Universal Service Reform Act of 2010 contains a number of program modifications that we support. Among the modifications we support, the bill:

- Maintains rate of return regulation for eligible communication service providers;
- Defines universal service to include high speed broadband service, so support for the deployment and operation of broadband networks will be explicit;

- Requires contribution to the Universal Service Fund from a wider range of providers, including all broadband providers;
- Requires the Federal Communications Commission (FCC) to act on intercarrier compensation reform in the near term and allows the Universal Service Fund growth factor to accommodate any intercarrier flows directed to it;
- Addresses so-called “phantom” traffic by mandating identification of all calls;
- Prohibits implementation of a primary line restriction;
- Includes requirements to ensure audits are fair and auditors are trained in universal service fund program compliance;
- Eliminates the so-called “parent trap” so that providers acquiring exchanges are not stymied from investing in such markets;
- Maintains current Act requirements on comparability of service in terms of price and scope as well as sufficiency of support; and
- Provides some relief from deployment requirements for high-speed broadband service to unserved areas where significant high-cost market conditions exist.

Addressing each of these modifications in further detail:

Rate of Return Regulation

H.R. 5828 maintains rate-of-return regulation for the recovery of costs and distribution of high-cost support to eligible communication service providers. Rate-of-return regulation represents a significant broadband deployment success story. Unfortunately, the National Broadband Plan recommends eliminating this regulatory framework that has enabled carriers operating in hard-to-serve, high-cost areas to install and maintain critical high-speed connections. The Universal

Service Reform Act of 2010 recognizes that rate-of-return regulation promotes highly desired investment in America's rural communications networks by providing stability to the carriers that serve these areas. In addition, under rate-of-return regulation, waste, fraud, and abuse are held in check and monitored regularly by regulatory bodies. Rate-of-return regulation is well-tailored for promoting responsible investment in broadband networks in rural America.

By contrast, price-cap regulation, which the National Broadband Plan proposes to replace rate-of-return regulation, tends to drive investment where risk is least and likelihood of recovery is greatest and quickest – in other words, toward more urban and densely populated markets. Price-cap regulation often provides little, if any, incentive to invest in many parts of rural America where the costs to deploy are highest and the customer base is small. As a result, price-cap regulation has proven far less successful in encouraging deployment of advanced communications infrastructure in rural America. If policymakers truly desire to promote ubiquitous deployment of state-of-the-art communications infrastructure, the rate-of-return form of regulation must be sustained as a foundation for broadband deployment.

Explicit Support for Broadband Deployment

Government policies and programs, including universal service, are instrumental in promoting affordable and comparable communications services for all. The United States public switched telecommunications network remains the envy of the world. The same should hold true as this network transitions toward provision of broadband services. While rural carriers have taken significant steps to deploy broadband already, more remains to be done, and the Universal Service Reform Act of 2010 takes an important step by declaring broadband to be a universal service.

While technological advances may help to reduce some costs associated with broadband deployment, it is still always going to be more expensive to serve rural America due to low population density, expansive distances, and often-rugged terrain. Without federal policies such as universal service to ensure adequate and predictable cost recovery mechanisms for broadband, our national goal of universal broadband access may never be realized.

Contribution Expansion

The bill would assess contributions on any entity that currently pays into the Universal Service Fund, any provider of a service that uses telephone numbers or IP addresses to provide voice communications, and any provider that offers a network connection to the public. We support efforts to broaden the contribution base, and we believe that all those who enable users to access networks should contribute to the Universal Service Fund. Expanding the current universal service programs to include broadband as a supported service without also requiring broadband services to contribute to universal service would undermine the goal of providing affordable, robust, and reasonably comparable broadband access service to all Americans.

Intercarrier Compensation

The bill would give the FCC authority to reform both interstate and intrastate intercarrier compensation, and directs the agency to act on such reform within one year of enactment of the bill. It also states that the FCC may recover intercarrier compensation revenues through an alternative recovery mechanism.

Intercarrier compensation was developed to help ensure that local exchange carriers can obtain sufficient cost recovery from other providers for use of the network. Such compensation is an essential part of operating and maintaining local connections to consumers. While we recognize the need for intercarrier compensation reform, the complete elimination of intercarrier compensation systems – which in many cases account for about one-third of rural telephone company revenue – would have a devastating impact on the ability of such providers to sustain operations and investment. H.R. 5828 takes a reasonable approach to this issue, allowing the FCC to direct that costs traditionally recovered via intercarrier compensation may be recovered via the universal service system in the future.

Traffic Identification

The Universal Service Reform Act of 2010 requires carriers to identify all traffic on their networks and requires all carriers to pass through that identification to ensure appropriate payment of intercarrier compensation. Our organizations support this effort to eliminate so-called “phantom traffic,” which has substantially undermined the proper application and operation of the existing intercarrier compensation framework. We believe the time has long since come for policymakers to act on this matter in order to stem any further hemorrhaging of compensation as a result of phantom traffic.

Audits

The Universal Service Reform Act of 2010 directs the FCC to use appropriate audit methodology and auditors specifically trained in universal service fund program compliance. We recognize the fundamental role that audits can play in the oversight of policies and programs if they are conducted appropriately and responsibly. Unfortunately, the existing audit process has proven burdensome, and its costs appear to far outweigh its benefits. This failure was outlined by the February 12, 2009 report from the Universal Service Administrative Company (USAC) that explained the audit’s shortcomings in terms of costs, approach, findings, and reporting. The USAC report noted how over the course of approximately three years, tens of millions of Universal Service Fund dollars have been spent to conduct more than 1000 separate audits – funding which could have been better used to enhance broadband deployment in high-cost areas. Yet, even more telling, is that all these dollars later, the audit reports have identified no instances of fraud or gross non-compliance within the high-cost portion of the program.

In apparent recognition of the need to improve these processes, the FCC recently took preliminary steps in conjunction with USAC to modify its audit approach. We support the efforts of this Subcommittee, and the provisions included in this bill, to help ensure that the FCC uses appropriate audit methodologies and processes, and reports factual program information to Congress and the public in the future.

Elimination of the "Parent Trap"

We support elimination of the FCC's "parent trap" rule that forces carriers acquiring exchanges to receive support based on the level of support, if any, that the previous owner/carrier received. This policy limits the ability of carriers to invest in areas that may drastically need such investment. Elimination of the parent trap may make it more cost effective for carriers, in particular, small, rural carriers, to acquire and improve service to areas where quality service is currently not available.

Comparable Access in Rural, High Cost Areas

The National Broadband Plan (Plan) sets a national goal of four Mbps, but also announced a primary goal to provide 100 Mbps to 100 million households. Our nation has had a long-standing commitment to ensuring that reasonably comparable communications services are available to all Americans. But if the Plan's goals are implemented as announced, they could result in a digital divide between the 100 million (likely urban or suburban) households receiving 100 Mbps and those in high-cost, rural areas that would receive speeds 25 times slower. H.R. 5828 rightfully commits to just, reasonable, and affordable rates, and comparable services for all regions of the Nation. Specifically, the bill reaffirms that all consumers should have access to telecommunication and information services and rates that are reasonably comparable to those services provided in urban areas.

Primary Line Restriction

We support the bill's prohibition on restricting universal service support only to a primary line connection. Congress has rightfully declined to limit universal service support to primary lines on several occasions – such a limitation would be inconsistent with the underlying reality that telecommunication providers build and maintain networks rather than a patchwork of individual lines and connections. There is an overall cost to building a network, and limiting cost recovery to only a few singular elements of the overall infrastructure would grossly underestimate the

actual costs of deployment – leaving carriers and their consumers to make up the dramatic difference.

Rural small businesses would be particularly vulnerable to such limitations. A primary line restriction would limit the ability to recover the high costs associated with providing telecommunications services in rural areas. This would put rural businesses at a distinct disadvantage to their urban counterparts and is unfair to residential consumers as well.

Rural wire-line carriers rely on this support, and the restriction would dramatically reduce incentives for the deployment and upgrade of facilities in rural areas. Moreover, because of its artificial limits on cost recovery, such a restriction could jeopardize the ability of rural carriers to service debt for and continue to operate already constructed plant facilities.

Eligibility Waivers

Rural carriers have made substantial strides to deploy broadband in the areas they serve – despite the fact that these areas represent some of the highest-cost, hardest-to-serve locations in the country. A National Exchange Carrier Association survey indicated that rate-of-return carriers participating in its traffic-sensitive pool had deployed DSL-capable broadband networks to 92% of their subscribers on average as of 2009. This is consistent with the long track record of investment by rural providers in their communities, and rural providers are eager to deliver even higher bandwidth services to their customers going forward. In fact, rural carriers have a history of taking every reasonable step to provide state-of-the-art communications infrastructure and services to their consumers. They are invested in their communities, and they are not expending effort to figure out how *not* to serve their friends, neighbors, and communities. For example, it was the rural sector that first completed the migration from multi-party to single party voice systems. It was the rural sector that first completed the transition from analog to digital. It was the rural sector that embraced wireless, fiber and a host of other technological and service advances ahead of other sectors of the industry. Why? Because doing so represents the very core of their mission – that is why they exist – to provide their consumers a service, not simply to generate profits. To put it another way, they exist to ensure rural Americans can access the same

economic, educational, health care, and personal opportunities Americans in every other region enjoy.

Yet, geographic, technological, product availability, and economic considerations dictate that rural carriers operate in a common sense and judicious fashion. At times, the costs to reach individual customers or a given area may be so high that they limit or altogether preclude investment at a given point in time in the broadband networks necessary to serve the affected customers. The authors of this legislation have taken proper account of this reality.

The waiver mechanism in the bill ensures that core statutory universal service principles will be upheld by promoting deployment of broadband on as widespread a basis as possible – while also recognizing that, even with best efforts, carriers operating in very high-cost areas may not be able to provide the speeds and types of services that will ultimately be required by the FCC to some small sliver of their subscriber base. Such a framework is particularly important given that the exact standards are still to be developed by the FCC in implementing this bill, and we therefore do not yet know what speeds and availability commitments would be required under a revised universal service program. Without the automatic waiver for very high-cost areas as contained in the current version of the bill, a rural carrier could make every possible effort to reach 100% broadband availability, fall only a handful of customers short of that standard because of the high-cost nature of the area it serves, and still lose essential universal service support. Not only would such a drastic loss of support be counterproductive in trying to reach the remaining unserved customers, but it would also threaten the ability of the provider to operate and maintain the substantial investments made in getting to 97%, 98%, or 99% network penetration. This automatic waiver for very high-cost areas is therefore critical to allow providers in such areas to operate and invest without fear that a minor shortfall in availability could result in a grievous loss of support – a loss that will undermine their ability to continue serving the overwhelming majority of customers to whom they have delivered broadband.

Areas of Concern

In the opening part of this testimony, I referred to this bill as a laudable effort at finding common ground on very difficult issues, and for that reason, our organizations endorsed the bill. This being said, a few provisions of the bill cause concern for small, rural telecommunication providers. As representatives of these providers, we are obligated to identify and express these concerns. Two provisions in particular are worth noting:

- Reducing or eliminating high-cost support in “competitive areas”; and
- Implementation of a new, unproven cost model that may not permit rural providers to meet universal service goals of providing reasonably comparable and reliable service in high-cost areas.

Reducing or Eliminating High-Cost Support in “Competitive Areas”

The bill proposes to reduce or eliminate altogether high-cost support in certain portions of those areas where at least 75% of the households can purchase wireline voice service and wired high-speed broadband service from an unsupported, facilities-based, non-incumbent provider. Many of the details of this proposal, such as how exactly areas will be apportioned and the process for “losing” and/or “re-obtaining” universal service support, are left for the FCC to develop in subsequent rulemakings. This uncertainty is of significant concern to rural providers, and could have the unintended consequence of hindering investment in broadband networks in the near-term.

Moreover, rural providers are particularly concerned that this proposal could lead to a dramatic loss of the support needed to continue operating and meet obligations to serve customers in high-cost areas. For example, the bill precludes imposition of carrier-of-last-resort obligations on the non-incumbent provider in a “competitive area.” This indicates that the incumbent will therefore continue to bear carrier-of-last-resort obligations in that competitive area, even as it may now receive little or no funding for bearing and living up to that obligation.

The carrier-of-last-resort obligation is essential to ensuring that service is available in rural areas. It effectively compels a carrier to keep or make network facilities available for customers in places where there might otherwise be no business case to do so. Even if a facilities-based competitor may enter a market (thus prompting a potential loss of support for the existing provider), this does not mean that the competitor will necessarily be there forever or operate throughout the entire area it once indicated it would serve. Companies rise and fall all the time, and what may look initially promising for entry into a new market often may not prove out over the longer term. If there is no carrier-of-last-resort backstop and no recognition of the support needed to ensure that the carrier-of-last-resort can live up to such obligations, we may find that rural communities are left in part or in whole with no one to turn to for broadband service. Any attempt to reduce or eliminate support in “competitive areas” must therefore be carefully coordinated and reconciled with the essential function that carriers of last resort will continue to play throughout rural America.

The Cost Model Proposal

As the industry is changing, so too is the manner of its cost recovery. The pressure to push direct consumer rates higher – to levels rural consumers can ill afford – is nearing a breaking point. The formula upon which intercarrier compensation has historically been based is undergoing extreme upheaval as communications minutes and types of traffic decrease and evolve. And the efforts to address these issues arise against a backdrop of simultaneous and contradictory pressures to both expand the universal service program (to support broadband deployment) and contract it (to control costs).

The costs associated with providing communications services to consumers are not decreasing. Indeed, quite the contrary is true as carriers move to deploy and maintain equipment that responds to the increasing network capacity demands of consumers. Some contend, however, that fund growth can be constrained by using a cost model to drive particular kinds of network investment that may be perceived in the abstract as more efficient. Unfortunately, as rural carriers expressed in comments recently filed with the FCC and as congressional policy-makers

themselves have raised in years past, cost models generally fail to capture the nuances and unique characteristics of different companies operating to serve different population densities in different topographical and geographic environments.

We raise this concern to underscore once again that there is far more to this debate than merely attempting to set a competitively neutral stage or to limit costs that are already monitored and strictly audited. We agree that steps should be taken to ensure that universal service funds are used in the optimal manner and consistent with the public interest. However, it is crucially important to point out that the public interest includes living up to our statutory universal service responsibilities, which include the provision of reasonably comparable services and the resolve to provide such services in a ubiquitous manner – more directly, to provide comparable services to all and in all areas, rather than focusing only upon those customers and portions of serving areas that are the least economically challenging.

Conclusion

Mr. Chairman, I want to thank you again for inviting me to be here. Your knowledge of the industry and your commitment to strengthening advanced communications in both urban and rural America make us all fortunate to have you serve on this Subcommittee.

The bill we are discussing here today is the product of many years of hard work for this Subcommittee. We look forward to continue working with you to move and improve this important bill going forward. In addition, I look forward to answering any questions you or your colleagues may have.

Mr. BOUCHER. Thank you very much, Ms. Bloomfield. And we look forward to continuing our work with you.

Mr. Davis?

STATEMENT OF STEVEN DAVIS

Mr. DAVIS. Good morning, Chairman Boucher, Ranking Member Stearns, and members of the committee. I appreciate the opportunity to express Qwest's views this morning on the Universal Service Act of 2010, a bill which we do endorse.

Qwest provides voice, data, Internet, and video services nationwide and globally and provides local telephone and high-speed Internet service in 14 western States. We provide approximately 10 million telephone lines and approximately 3 million broadband lines and currently have broadband service available to more than 85 percent of our customers.

Earlier this year, Qwest and CenturyLink announced their intent to merge. The merger will result in a combined company that will provide voice and broadband services in 37 States and operate a national 180,000-mile fiber network. The post-merger company will have over 17 million telephone lines and serve over 5 million broadband customers.

It is expected that the strong financial position of the combined company will enable it to make more broadband investment in the vast rural areas which it will serve. However, irrespective of the company's size, there will remain many high-cost areas that are simply uneconomic to serve without financial support.

Qwest's territory, like that of CenturyLink and other midsize carriers, includes many rural communities with very low household density. For example, in Douglas and Gillette, Wyoming, Qwest serves customers with local loops more than 75 miles long. The cost of running basic telephone service and broadband service in these areas greatly exceeds the revenue opportunity. Yet the existing universal service program often fails to provide the support necessary to make these areas economic to serve. Reform is needed, and Qwest commends Chairman Boucher and Congressman Terry for their leadership in addressing this very difficult issue.

The greatest flaw in the existing high-cost program is the use of State-level averaging to determine support. The current mechanism allocates high-cost support only if a company's average costs statewide exceed a national benchmark rate. As a result, many of the Nation's most sparsely populated communities served receive no Federal high-cost support whatsoever. So in Comstock, Minnesota, and Leonard, North Dakota, where Qwest's cost of serving customers is over \$200 a month and local rates are around \$20 a month, we receive no Federal high-cost support. There are hundreds of other examples.

The existing funds assumption that Qwest can overcharge customers in larger cities to subsidize the low-cost prices in rural areas is the product of a long-past monopoly environment. Therefore, we support the bill's targeting of high-cost support to wire center and subwire center areas, which will result in support being efficiently targeted to truly high-cost areas.

The bill also recognizes that support is inappropriate in areas where facilities-based competition exists. We agree. But sufficient

high-cost support must be provided for the higher-cost areas where the competitor does not offer service. The bill anticipates this scenario.

Qwest also strongly supports the provisions prohibiting traffic pumping, a harmful and illegitimate scheme that is costing the communications industry and consumers millions of dollars every year. Qwest appreciates that the bill's sponsors are addressing this serious issue.

Additionally, Qwest supports the bill's provisions addressing phantom traffic by requiring identification of traffic that originates on a carrier's network and requiring intermediate carriers to pass through that identification information.

Intercarrier compensation reform is also desperately needed, and a legislative mandate for the FCC to move forward and accomplish that reform may be the impetus we need to jump-start that process.

Qwest also agrees with Chairman Boucher, Congressman Terry, the FCC, and others that it is time to explicitly and directly support the deployment of broadband-capable networks to unserved areas through a modified universal service program. Therefore, Qwest supports the bill's explicit authorization of universal service support for the provision and maintenance and upgrading of broadband service. And I commend the work of the FCC in developing and drafting the National Broadband Plan.

As the bill requires, broadband universal service obligations, including carrier-of-last-resort obligations, should only extend to the areas for which broadband universal service support is provided. And in replacing existing support, we urge the Congress and the FCC to recognize the importance of a reasonable transition mechanism.

In drafting this bill, Chairman Boucher and Congressman Terry have provided Congress with a means to create a new and improved program for supporting universal service and access to basic telephone service and high-speed broadband service throughout America. And they have proposed additional reforms to intercarrier relationships that will result in fairer responsibilities for customers and carriers alike.

Qwest greatly appreciates the subcommittee's attention to these issues and renewed efforts to accomplish this much-needed reform. Thank you again for the opportunity to testify.

[The prepared statement of Mr. Davis follows:]

BEFORE THE HOUSE COMMITTEE ON ENERGY AND COMMERCE

**SUBCOMMITTEE ON COMMUNICATIONS,
TECHNOLOGY, AND THE INTERNET**

Hearing on H.R. 5828, “Universal Service Reform Act of 2010”

September 16, 2010

TESTIMONY OF ROBERT STEVEN DAVIS

**SENIOR VICE PRESIDENT
PUBLIC POLICY AND GOVERNMENT RELATIONS
QWEST COMMUNICATIONS INTERNATIONAL INC.**

Good morning Chairman Boucher, Ranking Member Stearns, and Members of the Committee. My name is Steve Davis, and I am Senior Vice President for Public Policy and Government Relations for Qwest Communications International Inc. Today I am here on behalf of Qwest Corporation, which operates as an incumbent local exchange carrier (ILEC) in fourteen mid-western and western states and Qwest Communications Company, LLC, which operates a long-haul long-distance network and one of the world's largest Internet backbones. I appreciate the opportunity to share Qwest's views on House Bill 5828, Universal Service Reform Act of 2010, a bill endorsed by Qwest, and reform of the federal universal service fund (USF) with you at today's hearing.

I. About Qwest and the CenturyLink/Qwest Merger

Before I address the bill and universal service issues directly, I would like to tell you a bit about Qwest and why these issues are so important to us. Qwest provides voice, data, Internet and video services nationwide and globally. Qwest provides service in Arizona, Colorado, Idaho, Iowa, Minnesota, Montana, Nebraska, New Mexico, North Dakota, Oregon, South Dakota, Utah, Washington, and Wyoming. Its service territory in these fourteen states encompasses 272,000 square miles. As of December 31, 2009, Qwest provided approximately 10.3 million voice grade access lines and approximately three million broadband lines to customers in its territory¹ and currently has broadband available to more than 85% of its customer base.

In April of this year, Qwest and CenturyLink announced their intent to merge the two companies. The merger is expected to close in the first half of 2011 and result in a

¹ Form 10-K of Qwest Communications International Inc., filed with the U.S. Securities and Exchange Commission, Feb. 16, 2010, at 2.

combined company that will provide voice and advanced telecommunications services in 37 states and operate a national 180,000 route mile fiber network. The post-merger company will have over 17 million telephone access lines and serve over five million high-speed internet customers. It is expected that the strong financial position of the combined company will enable it to make more investments to deploy broadband in the vast rural areas it will serve and push faster broadband speeds to more rural areas where there is a business case to do so. Even so, there will remain rural areas within the combined company service areas that will be uneconomic to serve without additional support.

Qwest's and CenturyLink's ILEC territories include many rural communities and areas of low household density. In many cases the low density areas the companies serve are also an extended distance from the nearest town. In areas of low household density, the companies experience low loop density and loops of extremely long length. In fact, Qwest has 175 wire centers with local loop density of fewer than ten access lines per square mile.² As an example of long loop lengths, in the wire centers of Douglas, Wyoming and Gillette, Wyoming, Qwest serves customers with local loops more than 75 miles long.

Qwest and CenturyLink are not alone. The extremely rural nature of many mid-sized companies' wire centers significantly increases their costs of providing basic local telephone service and broadband service in these rural areas relative to the costs for

² By contrast, within the Washington, D.C. city limits there are approximately 10,000 access lines per square mile. Washington, D.C. proper is 68.3 square miles. http://en.wikipedia.org/wiki/Washington,_D.C. Verizon has reported 668,803 access lines in D.C. to NECA. The NECA file is available at the following link: <http://www.fcc.gov/wcb/iatd/neca.html>. The file from the 2007 Report is in the zip file USF08R07.zip and the file within the zip is USF2008LC08. The switched access line count for Verizon of DC is in cell R990.

providing these services in more urban areas. This is due to several factors. The low density of rural areas results in increased costs per customer access line as fixed costs are spread over fewer lines. And, the extremely long loop lengths result in significantly increased costs to place and maintain the physical plant from the central office to the customer's premises. Still further, for Qwest, the rocky and mountainous terrain as well as significant lake regions that are encountered in much of its ILEC region and in which it is harder to place and maintain physical plant, also drives up the cost of providing basic telephone service to customers in those areas. CenturyLink and other mid-sized carriers face similar challenges.

And, the companies face robust competition in providing communication services throughout their ILEC regions. In each state in Qwest's ILEC territory, state regulators have found that there is sufficient competition in the provision of telecommunication services to afford reduced regulation or full deregulation of those services. But that competition tends to be concentrated in more urban areas, thus leaving the obligation to serve the higher-cost rural areas to the ILEC.

These carriers frequently receive insufficient universal service support to provide service in these challenging conditions. Despite the extremely rural nature of Qwest's service territory, Qwest receives less than 1% of the federal funds allocated to support rural facilities deployments, and less than 6.7% of the federal funds allocated to non-rural companies. Although Qwest serves extremely rural areas in all fourteen of the states in its ILEC territory, Qwest only receives high cost support in four states: Montana, Wyoming, Nebraska and South Dakota.

Further, the high-cost funding that Qwest receives supports only voice services and does not support Qwest's broadband deployment activities. This is evidenced by the fact that Qwest's high-cost support is less than its total costs to provide, maintain and upgrade its facilities for voice services in the wire centers for which it receives high-cost support. Additionally, the FCC's non-rural High Cost Model, which develops forward-looking costs for determining the size of the non-rural fund, is based on a voice-service-only architecture, and thus calculates non-rural costs without including facilities necessary for broadband deployment.³ Qwest's use of its high-cost support is also consistent with the statutory requirement that all support received must be used "only for the provision, maintenance, and upgrading of facilities and services for which the support is intended." 47 U.S.C. § 254(e). Currently, broadband is not defined as a supported service under the existing high-cost mechanism.

II. Qwest Endorses the "Universal Service Reform Act of 2010"

First and foremost, Qwest commends Chairman Boucher and Congressman Terry for their leadership in addressing the much-needed reform of the universal service program. As Qwest has previously stated, we endorse Chairman Boucher and Congressman Terry's bill. Qwest supports not only the universal service reform provisions of the bill, but also the provisions addressing intercarrier compensation obligations.

A. Qwest Supports the Bill's Targeting of Universal Service High-Cost Support To Wire Centers and Sub-Wire Centers

³ In contrast, the rural high-cost loop fund is based on embedded costs and includes the costs of fiber loop and loop electronics that provide broadband services.

To the credit of its sponsors, the bill would allow for the targeting of federal high-cost support to wire center and sub-wire center areas. Qwest fully supports this approach.

Since its inception, the mechanism for distributing high cost support to “non-rural” carriers has been ineffective in distributing support and achieving the universal service goals of the Telecommunications Act of 1996. Any new mechanism for distributing high-cost support must not replicate the errors of that mechanism. The greatest flaw in the existing non-rural high-cost program is the use of state-level averaging to determine support.⁴ The current mechanism allocates high-cost support to “non-rural” carriers in each state based on whether the ILEC’s statewide average costs exceed a national benchmark. Even if a carrier serves several high-cost areas in a state, if its average costs statewide do not exceed the national benchmark, no high-cost support is available for that carrier in that state. As a result, today, many of the nation’s most sparsely populated communities served by “non-rural” ILECs like Qwest receive little, if any, federal high-cost support. At the local level, Qwest and other “non-rural” ILECs serve thousands of rural wire centers with very high costs -- as calculated by the FCC’s High Cost Model⁵ -- yet receive little, if any, explicit federal support for those wire centers. For example, Qwest serves Patagonia, AZ (model monthly cost \$127 per line), Deckers, CO (model monthly cost \$137 per line), Rose Hill, IA (model monthly cost \$162 per line), Comstock, MN (model monthly cost \$221 per line), and Leonard, ND (model monthly cost \$204 per line), but receives no federal high-cost support in any of these areas. Currently, the national average cost developed by the FCC’s cost model is

⁴ The rural program has the parallel flaw of using study area averaging and masking high-cost areas within the study area.

⁵ The High Cost Model is the model used to calculate the forward-looking costs of non-rural carriers used to determine high-cost support to those carriers.

\$21.43, and high-cost support is available where a non-rural carrier's statewide average cost per line exceeds two standard deviations of this national average, or \$28.13 (the national benchmark). Clearly, all of the costs noted above well exceed this national benchmark, but because statewide average costs – and not individual wire center costs – are measured against the benchmark, none of these wire centers receives federal high-cost support. There are hundreds of other examples of Qwest wire centers and those of other mid-size carriers with costs above the national benchmark where no federal high-cost support is received.

The current use of statewide average costs to allocate high-cost support assumes that low-cost urban areas can subsidize high-cost areas. But, competition today in urban areas does not allow support to flow to high-cost areas. In today's competitive marketplace, a different allocation method must be adopted to effectively and efficiently target high-cost support to high-cost areas. Thus, Qwest fully supports the bill's requirement that the new cost model for determining and distributing high-cost support should have the ability to calculate costs of and target support to wire center and sub-wire center areas. For each wire center, the model should also be able to distinguish the costs for the higher-density core area of the wire center from the less dense areas outside the core.

B. High-Cost Support for an Incumbent Provider Must Be Maintained Wherever An Unsubsidized Competitor is Not Offering Service

The bill also directs the FCC to implement a mechanism for reducing or eliminating high-cost support to incumbent carriers in areas where at least 75% of households can purchase voice and high-speed broadband service from an unsupported, facilities-based, non-incumbent provider. The premise that high-cost support should not

be offered to one wireline competitor where another unsubsidized wireline competitor extensively offers comparable services is reasonable. But, high-cost support must be provided for the higher cost areas where the unsubsidized competitor does not offer service. And, that support, which cannot be recovered through prices for supported services, must be provided consistent with the high costs to provide service to these customers..

Qwest agrees that developing a mechanism for evaluating the continued need of high-cost support in competitive areas is critical. Such a mechanism should help reduce inefficient use of high-cost support and re-direct those monies to more efficient uses such as broadband deployment to unserved areas or providing support to high-cost areas that currently receive no support due to state-wide averaging. Any process implemented should be a consistent approach that applies to high-cost support for both “rural” and “non-rural” carriers. Each step of universal service high-cost support reform should move away from the “rural” carrier versus “non-rural” carrier distinctions and move towards a consistent approach to support based on the nature of the area served.

As the bill drafters have recognized, under any approach for eliminating high-cost support where it is not needed, sufficient support is required for every customer location that does not have an unsubsidized wireline competitive alternative. Absent a demonstration by the petitioner that unsubsidized wireline providers offer service to every customer location in the high-cost area, high-cost support for the area should not be wholly eliminated. Otherwise, Congress and the FCC run the risk of unintentionally reducing universal access to critical telecommunications services in high-cost rural areas.

High-cost support must be provided to the sub-wire center areas that the unsubsidized wireline competitor does not serve.

C. Qwest Supports the Bill's Prohibition of Traffic Pumping.

Qwest strongly supports the bill's provisions prohibiting traffic pumping. The bill prohibits a local exchange carrier from recovering access charges where it has a business, financial or contractual relationship with an entity pertaining to switched access revenues generated from services that the entity is offering for "free" or below cost. Traffic pumping is a harmful and illegitimate scheme that is costing the communications industry and consumers millions of dollars each year. Qwest fully supports immediate steps to clearly legislate the illegality of these activities.

Traffic pumping arises from business relationships between small local exchange carriers (LECs) and providers of competitive non-regulated services such as conference calling and chat rooms. The scheme works like this. The FCC's current rules allow these small LECs (generally rural LECs) to tariff very high interstate switched access rates because the rules assume that the LECs will have low traffic volumes and high per unit costs. The LEC's business partner (often referred to as a "Free Service Provider" or FSP) offers the conference calling, chat room or other competitive services for free, with these services accessed via toll calls to numbers assigned to the small LEC. These FSPs are not actual customers, and do not order or pay for any telecommunications services from the LEC. The small LEC's traffic volumes skyrocket (often from a few thousand minutes per month to millions of minutes per month), its per-unit costs dive, and massive profits roll in from access charges paid by interexchange carriers ("IXCs"). The FSP finances its "free" operations via kickbacks from the LECs in the form of sharing of the high access

charges. To the extent that the LEC tariffs do not allow for charging switched access on traffic not destined for an end-user customer who purchases services, the traffic implicated in the traffic pumping scheme is not switched access, and the tariff does not apply. However, as traffic pumping LECs become more sophisticated, they are filing tariffs which include traffic to non-customers as eligible for switched access charges.

The scheme works because of several economic and regulatory quirks, the two most significant of which are:

- First, the small LECs' termination of toll calls to the FSPs is a monopoly service. Whether the LEC is an incumbent LEC or a competitive LEC, it terminates all calls to the numbers assigned to the FSPs. Thus, IXC's cannot avoid routing traffic to the traffic pumping LECs and cannot seek to deliver traffic via a LEC with reasonable access rates.
- Second, the FCC's rules prohibit IXC's from avoiding the LECs' excessive charges by refusing to deliver the artificially pumped traffic to the LECs.

It has been estimated that traffic pumping costs to the economy could exceed \$500 million if the problem is not addressed.

Last year, the Iowa Utilities Board determined that intrastate access charges generated by traffic pumping were unjust, unreasonable, and unlawful under Iowa law.⁶ Fundamentally, with the exception of the traffic pumping LECs themselves and their FSP partners, there appears to be universal agreement that traffic pumping presents a serious danger to the telecommunications structure, competition and public welfare.

⁶ In re Qwest Communications Corporation v. Superior Telephone Cooperative, (Iowa Utilities Board September 21, 2009), Docket No. FCU-07-2.

Proposals have been advanced to prohibit traffic pumping. This bill proposes simply prohibiting the assessment of access charges in situations where the LEC and a FSP have a revenue sharing arrangement and the competitive service is offered below cost. A recent proposal by a coalition of IXC's, including Qwest, and others (including a provider of conference calling service that does not rely on a traffic pumping scheme and thereby faces unfair competition from those that do), proposed a methodology to the FCC that would bring LEC rates to reasonable levels once certain levels of minutes were processed per month per line.⁷ The FCC's rulemaking on traffic pumping has been ongoing for almost three years, and resolution of traffic pumping is designated as an important part of the National Broadband Plan. The Plan identifies traffic pumping as an issue that should be addressed in the relatively near future, and Qwest agrees that rules should be implemented as soon as possible to prohibit traffic pumping activities. Qwest appreciates that the bill sponsors are addressing this serious issue and supports the bill's proposed solution to the problem.

D. Qwest Supports the Bill's Provisions Requiring Identification of Traffic and Requiring the Commission to Address Intercarrier Compensation Reform

Requiring all carriers to identify traffic that originates on their networks and requiring intermediate carriers to pass through that identification information is a critical step in effectively addressing the variety of phantom traffic issues that are the result of no identification or mis-identification of traffic being handled by multiple carriers. Additionally, intercarrier compensation reform is desperately needed and a legislative mandate for the FCC to move forward and accomplish that reform may be the impetus

⁷ See Letter from Glenn T. Reynolds, Vice President Policy, USTelecom to Marlene Dortch, Secretary, FCC, WC Docket No. 07-135 (dated Aug. 31, 2010).

needed to jumpstart that process. Qwest is pleased that Chairman Boucher and Representative Terry have included these provisions in the bill.

E. Qwest Supports Universal Service for Broadband Services

In the National Broadband Plan, (Plan), the FCC estimates that 14 million people living in seven million housing units in the U.S. do not have access to terrestrial broadband infrastructure that can provide the Plan's target broadband service.⁸ Qwest agrees with Chairman Boucher, Congressman Terry, the FCC, and others that to accomplish the goal of universal availability of broadband service in the United States, it is time to explicitly and directly support broadband service, especially deployment of broadband-capable networks to unserved areas, through a modified universal service high-cost program. And, with the completion of the Department of Agriculture Rural Utilities Service disbursement of funds for broadband deployment under the American Reinvestment and Recovery Act, this is now even more critical. Universal service support is now the only remaining potential source of funding for broadband deployment to unserved and underserved areas. Qwest thus supports the bill's explicit authorization of universal service support for the provision, maintenance and upgrading of high-speed broadband service.

Reform is critical. The current high-cost program is already in need of significant repair and should be overhauled in order to explicitly and effectively support broadband-capable networks. Further, as the bill drafters have recognized, the current non-rural high-cost model is not designed to consider broadband network costs and in turn does not provide support that would enable non-rural providers to take on those costs in many

⁸ NBP, Chapter 8.1 at 136.

rural areas. To accomplish universal broadband service, new mechanisms that directly support broadband deployment to those areas must be designed and implemented.

And, there are other inefficiencies in the existing high-cost program that should be addressed and not perpetuated in reforming the program to support broadband. High-cost support to competitive carriers -- in areas that could not economically sustain one carrier -- has caused the fund to increase dramatically, while steering the fund well off its intended course of ensuring universal availability of essential communication services. Irrespective of whether it ever has, the high-cost program is not now providing support in a manner that effectively advances its fundamental goal of universal availability of essential communication services.

Congress and the FCC need to refocus high-cost support to broadband and voice services, target support to truly high-cost areas, and eliminate extraneous support so that, at most, not more than one provider of fixed service and one provider of mobile service is receiving support. To accomplish this, Qwest supports the bill's direction that the FCC develop a new cost model for calculating high-cost support that takes into account the cost of providing voice service and high-speed broadband service that would replace the existing methodology for rural and non-rural carriers. Additionally, Qwest supports the FCC's recommendation in the National Broadband Plan to establish a Connect America Fund (CAF) to support universal access to broadband and voice services, and believes there should be two CAF mechanisms: (1) a competitive bidding process to support broadband deployment to unserved areas and (2) a model for ongoing support of broadband and voice service in high-cost areas.⁹

⁹ For additional information regarding Qwest's views on this issue, see Qwest's comments filed July 12, 2010 in *In the Matter of Connect America Fund; A National Broadband Plan for Our Future; High-Cost*

As the bill requires, broadband universal service obligations, including carrier-of-last-resort obligations, should extend only to the area for which broadband universal service support is provided. Further, in designing the new distribution mechanism, the Commission should use *total* costs of providing *supported* services to determine ongoing support. In other words, all the costs of maintaining the network to provide voice services and broadband service at the targeted speeds and service quality level should be included. But, the costs of maintaining the network to provide broadband service at higher speeds and to provide video service should not be supported by the new fund.

But, in replacing existing support, Congress and the FCC must recognize that any sudden elimination of that support will significantly undermine those carriers' ability to invest in their networks. Before replacing existing support, the FCC must first design a new cost model for distributing support, and then a transition from legacy support can be determined. But, Congress should direct the Commission to promptly move forward with phasing out CETC high-cost program support that is not advancing universal service and refocus that support to effectively and efficiently promote access to broadband and voice services in high-cost areas.

The bill as currently drafted requires universal service fund recipients to offer broadband service at an FCC-determined minimum broadband speed throughout each service area in which it is receiving support within a specified time period either through the recipient's own infrastructure or through resale of satellite broadband services. But, as the bill drafters recognized, any obligation to deploy broadband service throughout a service area must be tempered by permitting reasonable technology and cost limitations.

Universal Service Support, Notice of Inquiry and Notice of Proposed Rulemaking, WC Docket Nos. 10-90 and 05-337, GN Docket No. 09-51, FCC 10-58, rel. Apr. 21, 2010.

Even with support for broadband deployment, certain areas will remain uneconomic to serve by wireline or wireless infrastructure. In those situations, a provider must be able to obtain a waiver of the service obligation. Thus, Qwest supports the bill's provisions authorizing a waiver of the requirement where offering broadband service would be technically or economically infeasible and authorizing an automatic waiver where a provider demonstrates that the cost per line of deploying broadband service is at least three times the nationwide average cost of providing the service.

F. Qwest Supports Reform of the Universal Service Contribution Methodology

The universal service contribution methodology needs to be simplified and restructured to better correspond with today's communication technologies and marketplace offerings. Because the marketplace has evolved to product offerings that often include packages and bundles of services providing interstate and intrastate telecommunications services and services that can be used as information services and/or telecommunications services, companies have had to adopt very complex administrative procedures to determine assessable interstate revenue. Further, the contribution factor, currently approximately 13% of assessable revenues, has become a significant fee for customers purchasing assessable services. It is also high enough to affect competitive pricing if one provider views a service as assessable and a competitor offering a similar service views that it is not assessable. Qwest thus supports the bill's providing the FCC with flexibility in designing a contribution methodology that will best resolve the myriad of problems with the current approach. In authorizing a broader base of contributors and the option to assess contributions on all communication service revenues, the bill gives

the FCC new tools that should greatly aid it in accomplishing effective contribution reform.

III. Conclusion

In drafting this bill, Chairman Boucher and Congressman Terry have provided Congress with a golden opportunity to adopt the successes and correct the errors of the current universal service high-cost program and structure a new and improved program for supporting universal access to basic telephone service and high-speed broadband service. And, they have proposed additional reforms to the universal service program and intercarrier obligations that should result in fairer responsibilities for customers and carriers alike. Qwest greatly appreciates the Subcommittee's attention to these issues and its continued efforts to accomplish this much-needed reform.

Thank you again for the opportunity to testify today on these important issues. I look forward to your questions.

Mr. BOUCHER. Thank you very much, Mr. Davis, and thanks for your thoughtful comments.

Ms. Grillo.

STATEMENT OF KATHLEEN GRILLO

Ms. GRILLO. Chairman Boucher, Ranking Member Stearns, and members of the subcommittee, good morning. And thank you for the opportunity to discuss the universal service reform bill introduced by Chairman Boucher and Congressman Terry.

Congress last updated the Universal Service Act in 1996, almost a decade and a half ago. A lot has changed since then. Now is the time to put in place the policies that will help expand the reach of broadband networks to all Americans. Verizon is pleased to endorse the Boucher-Terry bill and congratulates its authors on crafting legislation that has bipartisan and industry support.

Since the subcommittee's last hearing on this topic, the FCC has submitted its National Broadband Plan to Congress. Like the USF reform bill, it represents the culmination of thousands of hours of work. It is a thoughtful, comprehensive approach aimed at maximizing the boundless power of the Internet and ensuring broadband access for every American.

From our point of view, there are three priorities, and all of these issues are addressed in the bill before the subcommittee.

First, universal service reform. There is no doubt about the critical need to revamp the high-cost universal service program. The High-Cost Fund is literally at a tipping point. The program has doubled over the last decade, and just to subsidize traditional voice service in rural areas.

But plain old telephone service is rapidly becoming a thing of the past, and consumers demand much more. They want to surf the Internet, send e-mail, and download videos—and all over the same network connections. We must refocus the fund to reflect the way consumers live and work today.

And as the bill repurposes the USF for broadband, we must keep in mind that consumers pay for the fund through charges on their monthly bills, and charges must be in line with what consumers can reasonably afford.

As we have said before, the problem with universal service is not that we are spending too little money; it is that we are not spending it on the right services and in the right places. To that point, the bill takes an important step forward by putting in place a more rational, competitive bidding system for high-cost support to wireless carriers.

Almost everybody recognizes that the way wireless carriers receive support today is problematic. Among other things, multiple wireless providers get support in the same areas, even where other carriers compete without any universal service support at all. And the right competitive bidding system will fix these problems.

Second, intercarrier compensation. The system of charges between carriers for exchanging communications traffic is a mess. The current system is based upon distinctions which bundled services—phone, TV, and Internet access—have rendered meaningless. It is important to fix this broken system at the same time that the Universal Service Fund is updated. And the bill properly provides

a firm deadline, 1 year from enactment, for the FCC to complete intercarrier compensation reform.

And third, traffic pumping. The traffic-pumping scams that have plagued the industry in recent years must be stopped immediately. These scams have cost the industry hundreds of millions of dollars as so-called traffic pumpers game the current system by exploiting antiquated rules. This bill would appropriately cut off many of those scams.

And, lastly, I would like to say a word about one issue that isn't addressed by the bill: broadband adoption in low-income households. Representative Matsui and others are leading voices on this issue. And for most Americans, broadband is an affordable service that offers tremendous value. That said, the price of broadband service is a real issue for some households. Digital literacy, affordability of a computer, and relevance are also significant factors. The National Broadband Plan proposed that the FCC launch pilot programs to test alternative solutions, and Verizon supports that approach.

Thank you again for the subcommittee's continued leadership on sustainable universal service policies, and we look forward to working with the subcommittee as we move forward.

[The prepared statement of Ms. Grillo follows:]

Prepared Testimony of Verizon Senior Vice President Kathleen M. Grillo
U.S. House of Representatives Committee on Energy and Commerce,
Subcommittee on Communications, Technology, and the Internet
“Universal Service Reform Act of 2010”
Thursday, September 16, 2010

Chairman Boucher, Ranking Member Stearns, and Members of the Committee: Thank you for the opportunity to discuss the Universal Service Reform Act of 2010 introduced by Chairman Boucher and Representative Terry. Congress last updated the Universal Service Fund in 1996 – almost a decade and a half ago. A lot has changed since then. It’s now time to put in place the right policies that will help make broadband services even faster and further expand the reach of high-speed networks in America.

Three things happened since the Committee last heard testimony on universal service reform:

First, there is a bill. In July, following months of hard work and discussions with all sectors of the industry and others, Chairman Boucher and Representative Terry introduced the Universal Service Reform Act. Verizon is pleased to endorse the bill and congratulates the Chairman and Representative Terry on crafting legislation that has bipartisan and industry support.

Second, there is a plan. The FCC submitted the National Broadband Plan to Congress earlier this year. Like the USF Reform Act, the Plan represents the culmination of thousands of hours devoted to developing a thoughtful, comprehensive approach to maximize the boundless power of the Internet and ensure that all Americans are connected.

Third, the FCC is moving forward to implement national broadband priorities. The FCC has been acting on recommendations in the Broadband Plan. The FCC has also kicked off a number of other proposed rulemakings that track recommendations in the National Broadband Plan.

Now, three things must happen, all of which the bill before the Committee addresses. Let me talk a little bit about each of these priorities as well as other aspects of the Universal Service Reform Act itself. We commend Chairman Boucher and Representative Terry, who worked tirelessly on the bill to bring all stakeholders together and find consensus on these complicated issues. The result is legislation that would truly modernize the Universal Service Fund. All Americans have an interest in an up-to-date and sustainable universal service program.

First, universal service reform. There is no doubt about the critical need to revamp the high-cost universal service program. The high-cost fund is literally at a tipping point. The program grew significantly in recent years in order to subsidize traditional voice service in rural areas. But plain-old telephone service is rapidly becoming a thing of the past. Consumers demand a lot more from their communications providers. They want to make phone calls, send text messages, surf the web, exchange email, download videos, etc. – all over the same network connections, whether wireline or wireless. Many of the tasks that we once performed using paper (such as renewing a driver's license), or in person (such as consulting with medical professionals), are now performed using broadband Internet connections. We must change the focus of the Universal Service Fund and make it work for consumers in a way that reflects how we now live and work.

As we repurpose the USF for broadband we also should keep in mind that consumers pay for the fund through charges on their monthly bills. Whatever changes we make must be in line with what consumers can reasonably afford and must not reach a point where consumers rebel against the program. The National Broadband Plan makes clear that there are tough choices ahead and commits to reforming the fund within the amount spent for existing programs. Whether universal service reform comes from legislation or from the FCC, Verizon supports keeping the size of the fund manageable for consumers. This is important because the problem with universal service is not that we are

spending too little money; it's that we are not spending it on the right services in the right places. Both the Universal Service Reform Act and the National Broadband Plan could help fix that.

Second, intercarrier compensation reform. The system of charges and rates between carriers for handling communications traffic is a mess. We have to fix this broken intercarrier compensation system at the same time that we update the Universal Service Fund. Some carriers rely on both universal service and intercarrier compensation funding as their primary revenue. Changes to one source of revenue should consider changes to the other, so as to minimize negative consequences for investment in network upgrades and broadband deployment.

Moreover, it is not possible to maintain the current intercarrier compensation system in today's communications market. The current system is based on the idea that there are meaningful distinctions between interstate and intrastate services and between telecommunications and information services. The result of these distinctions is the current patchwork of vastly different charges and rates for communications traffic depending on what the traffic is, where it came from, and where it is going. In a market where most consumers now purchase a bundle of any-distance services (such as phone, TV, and Internet access), these distinctions are meaningless. And even in situations where it is still possible to measure traffic in these ways, continuing to do that just for intercarrier compensation purposes does not make sense. All of these complications and uncertainty reduce investment in broadband.

Parties mostly agree that a single, low, uniform intercarrier compensation charge for terminating traffic on a network is the right solution. Carriers should also have the opportunity to rebalance their end-user rates. If they cannot recover lost access revenues from their customers, carriers could recover part of the difference during a transition period from a new universal service program.

The new USF intercarrier compensation program should be transitional and decline over time. And importantly, the new system should be a default system only. Carriers should be free to enter into different intercarrier compensation arrangements that make sense based on marketplace considerations.

Third, traffic pumping. We have to stop the so-called “traffic-pumping” scams that have plagued the industry the last several years. And we have to do it right now. These scams have festered for five years, costing literally hundreds of millions of dollars. With traditional traffic-pumping schemes, the traffic pumpers game the intercarrier compensation system by exploiting antiquated FCC and state rules. They form collusive arrangements to drive traffic way up in rural areas with historically low traffic volumes and correspondingly high access rates. Some local exchange carriers in these areas then partner with chat-line and other providers that market services as “free” and collect kickbacks from the LECs. The kickbacks are paid with access revenues from long distance and wireless carriers held hostage under the current system.

These scams are no different from illegal kickbacks involving regulated revenues in other industries. In the healthcare industry, for example, such kickbacks between healthcare providers and suppliers land people in jail. The intercarrier compensation rules that allow LECs to charge other carriers high access rates in rural areas are supposed to help consumers in these sparsely populated areas receive affordable and reliable service. The rules were never designed to enable these get-rich-quick schemes. And these are just the *old* traffic-pumping scams. Because traffic pumping has been allowed to fester for so long the schemes are evolving and becoming more brazen. We now know about new schemes involving wireless traffic that terminates to competitive local exchange carriers.

The time for talking about the nuances of traffic pumping is over. The dollars are huge, the scams are significant obstacles to universal broadband access, and the problems are getting worse the longer we wait.

Let me turn now to the Universal Service Reform Act. This is important legislation that moves the ball forward on the critical issues – universal service reform, intercarrier compensation reform, traffic pumping – and other matters.

The bill would transform the USF from a voice-based support system to a broadband system and help expand the reach of broadband services to those Americans who still lack access to high-speed networks. The bill also provides a firm deadline – one year from the time the bill passes – for the FCC to move forward with intercarrier compensation reform. That deadline is certainly workable. The pieces of intercarrier compensation reform are already in place, and a gentle push from Congress to get this issue over the goal line is just what we need. As well, the bill would cut off many of the traffic-pumping scams that are siphoning investments away from broadband.

In addition, the Universal Service Reform Act puts in place a more rational, competitive bidding system for high-cost USF support to wireless carriers. Almost everybody recognizes that today's system is broken. Among other things, multiple wireless providers get support in the same areas, even where there are carriers that compete without any universal service support at all. The right competitive bidding system will fix these problems. Competitive bidding will also bring the Universal Service Fund in line with established procurement procedures at other federal agencies.

The bill will also leave a number of important decisions to the FCC – the expert agency in charge of administering the fund and its various programs. Where the FCC comes out on these issues matters a lot and will determine whether the fund will shrink, grow, or stay about the same size.

For instance, the minimum download speed required to qualify as a broadband service is a significant metric that the FCC would need to set under the bill. The National Broadband Plan coalesces around a broadband speed target of 4 Mbps. There are divergent views about whether that target speed is too fast or too slow, but everyone recognizes that higher speeds require more network subsidies in rural areas. Likewise, the service area required for broadband deployment for both wireline and wireless carriers will directly impact the size of the fund and carrier business models. So will the number of carriers eligible to receive universal service subsidies.

Other questions remain. How the FCC implements the challenge proceedings to reduce LEC high cost support in competitive areas will determine whether that part of the bill results in a savings. Another part of the bill correctly directs the FCC not to burden consumers unreasonably when it makes changes to the program.

I'd like to close by talking about how to increase broadband adoption in low-income households – an issue not yet addressed in the bill but one that Representative Matsui and others are leading. For most Americans, broadband is an affordable service that offers tremendous value. That said, the price of broadband is a real issue for some households. In addition, digital literacy, affordability of a computer, and relevance are significant factors affecting broadband adoption. The National Broadband Plan and many parties have proposed that the FCC launch pilot programs to test out different alternatives. Verizon supports that approach.

* * *

Thank you for the opportunity to discuss these important issues and for the Committee's continued leadership on sustainable universal service policies. Verizon looks forward to working with the Committee and the FCC to move these matters forward.

Mr. BOUCHER. Thank you very much, Ms. Grillo.
Mr. Assey.

STATEMENT OF JAMES ASSEY

Mr. ASSEY. Thank you, Chairman Boucher, Ranking Member Stearns, Congressman Terry, and other members of the subcommittee. My name is James Assey. I am the executive vice president of NCTA, the National Cable and Telecommunications Association. I am honored to be with you here again and testify today in support of H.R. 5828, the "Universal Service Reform Act of 2010."

Mr. Chairman, as many of the other witnesses have already told us, we live in a communications marketplace today that is fundamentally different from the world that greeted policymakers in 1996. That was a world where industry was providing voice service over circuit-switched networks, a world where almost no one was on broadband, and only 23 percent of the country had dialup Internet access.

The world we live in today is definitely very different. We believe that it is time, and in many respects past time, for us to begin the process of transitioning away from a monopoly-era support program to a more modern, a more neutral, and a more forward-looking, high-cost support mechanism that will bring broadband service to unserved areas and to underserved populations.

We further believe that the FCC has provided us with a valuable resource in the National Broadband Plan, which synthesizes reams of data and helps us assess where we stand today, where we need to be, and what measures must be taken to ensure that our universal service system for the 21st century is efficient, effective, and maximizes the incentives for private investment in building broadband networks.

Roughly 9 months ago, when the president of NCTA, Kyle McLarrow, sat in this seat and testified on universal service reform, he suggested several elements that should be parts of any effort to reform universal service: first, that we must control the size of the High-Cost Fund to ensure that it does not impose unreasonable burdens on consumers or distort competition; second, that we must reduce or eliminate high-cost support in areas where it is demonstrated that service can be provided without support; third, that universal service support for broadband should be targeted to help extend capabilities in unserved areas that currently do not have broadband service; fourth, that the universal service contribution mechanism should be reformed to allow assessment based on telephone numbers or another appropriate mechanism that promotes stability and simplicity; and finally, that reform must reflect the modern-day principles of competitive neutrality with respect to eligibility for universal service support.

Mr. Chairman, we continue to believe that these principles are the right ones and believe that H.R. 5828 helps to advance these principles in many significant respects.

Chief among its virtues, the bill creates a permanent and ongoing mechanism to better calibrate high-cost support to current realities of a competitive marketplace by reducing or eliminating support in competitive areas. It also adds needed controls on the

growth of the fund by allowing the FCC to consider all net revenues that a provider may obtain and also by ensuring that reforms will not unreasonably increase the contribution burden on consumers.

In addition, we support the bill's efforts to complete intercarrier compensation reform within a year, to make broadband specifically eligible for universal service support without resorting to reclassification, to stating that USF support should be technology-neutral, and also including accountability provisions to ensure that moneys go where they are needed.

Mr. Chairman, in sum, we are confident that H.R. 5828 is a deftly crafted compromise that can serve to remove jurisdictional impediments and help propel the FCC and our Nation towards meaningful and lasting reforms. And we look forward to working with you and the other members of the subcommittee.

Thank you.

[The prepared statement of Mr. Assey follows:]

**TESTIMONY OF JAMES M. ASSEY
EXECUTIVE VICE PRESIDENT
NATIONAL CABLE & TELECOMMUNICATIONS ASSOCIATION**

on

**H.R. 5828
Universal Service Reform Act of 2010**

before the

**Committee on Energy and Commerce
Subcommittee on Communications, Technology, and the Internet**

**UNITED STATES HOUSE OF REPRESENTATIVES
WASHINGTON, D.C.**

September 16, 2010

TESTIMONY OF JAMES M. ASSEY
EXECUTIVE VICE PRESIDENT
NATIONAL CABLE & TELECOMMUNICATIONS ASSOCIATION

Good morning, Chairman Boucher, Ranking Member Stearns, and Members of the Subcommittee. My name is James Assey, and I am the Executive Vice President of the National Cable & Telecommunications Association. Thank you for inviting me today to testify today in support of H.R. 5828, the Universal Service Reform Act of 2010.

NCTA represents cable operators serving more than 90 percent of the nation's cable television households and more than 200 cable program networks. The cable industry is the nation's largest provider of residential high-speed Internet service, having invested more than \$161 billion since 1996 to build two-way, interactive networks with fiber optic technology. Cable companies also provide state-of-the-art digital telephone service to more than 22 million American consumers in urban, suburban, and rural markets – almost wholly without any universal service support. Cable operators are committed to expanding access to quality voice and Internet services, and the dramatic growth in cable broadband subscribers is evidence of their success in doing so.

The universal service program has long been a critical element of our communications policy, ensuring that all Americans have access to rapid and efficient communications services at reasonable rates – and it will remain a cornerstone of communications policy in the broadband era. As a major contributor to the federal universal service fund, the cable industry has a significant interest in universal service issues. We believe it is time to transition away from a monopoly-era support program and toward a more modern, neutral, and forward-looking high cost support mechanism that focuses on bringing broadband service to unserved areas and

underserved populations – and that the growth of local voice competition offers the opportunity for policymakers to make this transition.

NCTA endorses the Universal Service Reform Act of 2010 as a sound first step in modernizing the universal service program to bring it into the competitive era and refocus the program on broadband adoption and deployment where support is needed. H.R. 5828 recognizes that government subsidies are neither necessary nor appropriate in competitive areas where the marketplace is working. Building on a proposal NCTA filed last year with the Federal Communications Commission, the bill will establish a permanent mechanism for the FCC to reassess universal service support levels in competitive areas and reduce or eliminate support where adequate competition exists. The bill also recognizes the significance of resolving the difficult, but very important, issues surrounding intercarrier compensation reform.

When NCTA President Kyle McSlarrow testified on universal service reform before this Subcommittee in November 2009, he suggested that reform should encompass several elements: controlling the size of the high cost fund to ensure that it does not impose unreasonable burdens on consumers or distort competition; reducing or eliminating high cost fund support to areas where basic service can be provided without the support; providing universal service support for high-speed broadband facilities in areas that currently do not have broadband service; reforming the universal service contribution mechanism to allow assessment based on telephone numbers; and ensuring competitive neutrality in eligibility for universal service support. H.R. 5828 addresses each of these issues.

Importantly, the Universal Service Reform Act of 2010 includes a mechanism for the FCC to reduce or eliminate high cost support in competitive areas where the presence of one or more unsubsidized wireline competitors demonstrates that a universal service subsidy is no

longer necessary to support provision of services in that area. The bill reasonably defines a competitive area as a service area where more than 75 percent of households can purchase both wireline service and high-speed broadband service from a non-incumbent wireline provider, although we believe the bill should be clarified to state expressly that this test is satisfied in areas where two or more competitors combine to meet the 75 percent threshold.

This reduction mechanism permits direction of high cost support away from areas that the competitive market has shown do not need the support, helping to direct scarce funds to only those areas where voice and broadband service would truly be unavailable without subsidy. Because the bill requires the FCC to apply the mechanism on a “recurring” basis, the need for high cost support will be continually reassessed to take into account changes in competitive markets, ensuring that universal service support is always based on current needs and not historical market conditions that may no longer exist. To ensure that this mechanism fulfills its objectives, we respectfully suggest that the bill be revised to ensure that the “hold harmless” provision does not prevent the FCC from reducing or eliminating high cost support in competitive areas.

The Universal Service Reform Act of 2010 rightly brings universal service support into the 21st Century by retargeting funding to support broadband services. The National Broadband Plan declares that “[e]veryone in the United States today should have access to broadband services,” and the Universal Service Reform Act of 2010 represents a major step forward in accomplishing that laudable goal. We also applaud the bill for recognizing the special needs of tribal lands for continuing high cost support.

Significantly, the bill funds the deployment of broadband services to all Americans without requiring that broadband be classified and regulated as a Title II telecommunications

service. Spurring broadband deployment requires a regulatory climate that promotes private sector investment and innovation by providing certainty and eliminating all unnecessary regulatory burdens. Maximizing incentives for private investment in broadband will minimize the impact on consumers who ultimately contribute to the universal service fund.

As an essential corollary to providing universal service funds to support broadband, the bill clarifies that universal service mechanisms (including the assessment of contributions) should be competitively neutral, so as to neither “unfairly advantage one communications service provider over another” nor “unfairly favor nor disfavor one technology over another.” In support of competitive neutrality, the bill makes two important changes to the current universal service programs. First, it opens high cost programs to all communications service providers able to provide required services, rather than limiting participation to only telecommunications carriers. Second, it makes clear that a provider’s service area – the area where it must meet universal service eligibility requirements – is the area where the provider itself is licensed or authorized to provide services rather than the incumbent local exchange carrier’s territory. These are welcome changes that will allow the universal service program to focus on providing services to those in need, rather than on essentially irrelevant concerns about the type of provider or type of technology that brings those services.

The bill also includes provisions intended to ensure that the high cost fund is no larger than necessary. For instance, it directs the Commission not to “unreasonably increase the contribution burden on consumers” as the fund is repurposed to support broadband services. On the “demand” side, in determining the amount of high cost support a provider might need, the bill rightly gives the FCC authority to consider a provider’s net revenues from the provision of any services over its communications infrastructure. If a provider is, in essence, telling the FCC

that it must have a financial subsidy for its network to be able to provide services in a high cost area, it is only appropriate that the provider should be required to demonstrate its financial need based on all services it provides over that infrastructure. Providers should not be allowed to obtain a subsidy for providing some services over their network when the mix of all services over that network provides them with a reasonable profit even without the subsidy. Finally, the bill retains the provision in current law that focuses universal service support on services that have been subscribed to by a substantial majority of residential customers “through the operation of market choices.” This test appropriately ensures that the universal service program is focused on ensuring that consumers in rural and insular areas – particularly areas with no broadband – get access to service that is comparable to their urban and suburban counterparts.

The bill also recognizes the continuing importance of the E-rate and other universal service programs. In particular, while providing well-planned and much needed reform to the high cost programs, the bill appropriately does not alter or limit entities’ eligibility to receive universal service support for providing services to schools, libraries, rural health care facilities, or to low-income consumers. The universal service programs that assist these entities are important and deserve continuing support. The bill’s institution of new audit controls on these programs will ensure that the funds are appropriately spent.

As this Subcommittee well knows, universal service reform is a challenging issue. Any effort to address this subject is bound to require some compromises, and H.R. 5828 is no exception. For example, NCTA has long supported a cap on high cost support, but the cost model approach provided in the bill leaves open the question of the ultimate size of the high cost fund. We also believe that support for broadband deployment should be expressly limited to unserved areas. In addition, we support other legislative efforts, such as those introduced by

Representatives Matsui and Markey to modernize the Lifeline, Link Up, and E-rate programs. On balance, however, H.R. 5828 is a constructive, positive step forward in bringing much-needed reform to a universal service program that has gone too long without it, and NCTA is pleased to endorse the bill. We particularly appreciate the leadership of Chairman Boucher and Representative Terry on these important issues.

Thank you again for the opportunity to share our views with you today. We look forward to continuing to work with you as you proceed to consideration of the bill.

Mr. BOUCHER. Mr. Assey, thank you very much.

And thanks for the endorsements that were forthcoming today from all of our stakeholder private-sector witnesses. We appreciate your work with us and your support for the passage of this legislation, which reflects the results of that cooperative effort together.

Ms. Grillo, let me direct a question to you, if I may. One of the things that we are doing in the bill to save money is moving from the current system of providing USF support to wireless, which essentially qualifies all of the wireless carriers in an area that meet the threshold and the qualifications for support, so you could have multiple carriers receiving support, and we are moving away from that in this bill to a competitive bidding model, where no more than two winners could be awarded support in a given study area.

Have you done any cost estimating in terms of how much money we will save in terms of fund expenditures by moving to this competitive bidding model? At the present time, the wireless support is about \$1.5 billion out of a \$4 billion annual fund. Can you give us a sense of what the annual savings would be in terms of that wireless component if we move to this competitive bidding model?

Ms. GRILLO. We have looked at that. As you know, Verizon, in particular, has been a proponent of using competitive bidding. We used to call it "reverse auction." We actually developed a fairly comprehensive proposal when the FCC was looking at this a few years ago, and what we did at the time was we tried to come up with an estimate of, sort of, the proposal that we had and how much money that would save. And what we have done is, sort of, use that to look at the structure that the legislation sets up and, you know, sort of, use some of the assumptions we used then and also take into account some of the changes.

Some of it is difficult because there are provisions in the bill that the FCC will have discretion to interpret. But, bottom line, we think probably the higher end of the range would be \$500 million and probably the lower end would be about \$200 million.

Mr. BOUCHER. So that is savings of potentially as much as \$500 million, but at least as much as \$200 million, depending on various factors that we can't predict at this point.

Ms. GRILLO. That is right. That is right.

Mr. BOUCHER. OK. That is a pretty substantial savings, \$200 million on an annual basis, from just this one provision alone.

Ms. GRILLO. Right, that is just that one provision.

Mr. BOUCHER. Yes, OK. Well, thank you, Ms. Grillo.

Ms. Bloomfield, a question for you. We are, in this legislation, preserving the rate-of-return model, which is the current foundation for awarding supported universal service. And I know that your companies, those that you are speaking for today, are particularly interested in retaining this rate-of-return model.

Can you explain to us why keeping that means of providing support is so important to the rural carriers that benefit from USF?

Ms. BLOOMFIELD. Thank you, Mr. Chairman. I would be very happy to answer that question.

Rate-of-return regulation has actually really been part of the broadband success story in a lot of these rural markets. And what rate of return does is it allows the carriers to not get a guaranteed rate of return but it ensures that they are able to get some recov-

ery of their costs, of the capital expenses that they are putting into these rural markets when they build these networks. It gives them stability. It gives them predictability. It also recognizes the fact that they are carriers of last resort in these markets, that they are building out to the markets and edges of the market where nobody else actually wants to serve and take on those obligations.

It also is one of those forms of regulation that really does prevent waste, fraud, and abuse because it has a lot of oversight from the regulations and the regulators. And I think the other thing that is very important in contrast is the other form of regulation potentially could be price cap. And price cap is a form of regulation that really drives incentive to invest in those areas where it is lowest risk and you get the greatest return. Obviously, a lot of these rural markets, that is not an economic model that is efficient and that actually works.

Mr. BOUCHER. OK.

Ms. Matthey, I am going to ask if you want to engage on this subject. And I will set the foundation for this engagement. The Commission, as part of its National Broadband Plan, had suggested that there might be a movement from rate-of-return regulation as the basis for USF distributions to price caps.

And I would note that, in the provision we have placed in this legislation, we would retain the rate-of-return formula, but you could reduce administratively the rate of return that, in fact, is allowed. Today, it is a fairly high number. It is about 11.4 percent, as I understand it. And there is nothing in this provision that would prohibit you from reducing that percentage. If you thought that a lower number made sense, you could reduce it.

So my question to you is this: Given that tremendous flexibility to establish what the rate of return actually is based on investment, why is that not a sufficient model? Why would it not be appropriate to take that course, which Ms. Bloomfield has said is so important to the rural carriers in order to provide predictability and other necessary planning devices, when you are given the very broad flexibility to actually decide what the real rate of return is?

Ms. Matthey?

Ms. MATTEY. Well, certainly, as you say, the FCC, under current rate-of-return regulation, could change the rate of return. And, as well, the FCC could look at other rules that apply to the current receipt of universal service high-cost support for the rate-of-return carriers.

Mr. BOUCHER. OK. OK, fine.

My time has expired, and I am pleased to recognize the gentleman from Florida, Mr. Stearns.

Mr. STEARNS. Thank you, Mr. Chairman.

Ms. Matthey, I have here the report from the FCC called, "Comparison: Universal Service Fund Transformation Recommendations, August 2010." And I go to page 5, and it has the Boucher-Terry bill, talking about the size of the fund. And it has three or four comments. And one of the comments says, "The High-Cost Fund, not capped, may increase significantly."

Now, in the bill, they have the language that it can increase unreasonably—I mean charges can increase. There is no ceiling, there is no cap. It appears from what you are saying in this report—and

I need your comments—that you are saying the bill, as it is written today, will not control the cost of the Universal Service Fund.

Ms. MATTEY. Well, as I understand it, the legislation does direct the Commission to not unreasonably increase the contribution burden on consumers. And, of course, we would very much appreciate any direction from Congress as to what constitutes an unreasonable burden.

Mr. STEARNS. Well, Ms. Grillo pointed out accurately that the High-Cost Universal Service Fund has doubled over the last decade. At the same time, I think the unserved has not increased dramatically. So the question would be, since the fund is increasing, as Ms. Grillo mentioned, doubled over the last decade, you know, why does the fund keep going up?

And I think what many of us are worried about is, the way the language is in the bill and based upon what you are saying here, do you think the costs will increase dramatically again, like we saw in the last 10 years?

Ms. MATTEY. There are many reasons why the High-Cost Fund has increased over the last decade. Among the reasons are the loss of access lines that smaller carriers as well as larger carriers have incurred, as well as the growth in the funding provided to competitive ETCs.

The bill has provisions that would address how funding should be provided to competitive ETCs. And, therefore, it would depend very much on how the bill would be implemented, you know, based on the direction from Congress.

Mr. STEARNS. OK, but what you are saying here is that—your language here is that it may increase significantly. And, really, the purpose of the bill is to take and cap it and really decrease the cost so we can put it to broadband. I mean, that has been the underlying assumption that many of us have gone along with the bill, that if we can save money here, we will give it to broadband. As Mr. McCormick said, we have 95 percent of the market has up to 4 megabytes, I think Mr. McCormick said. We are looking at 5 percent, the last 5 percent.

And I would point out, this is true, but also the Departments of Agriculture and Commerce have not even finished off awarding \$7 billion in broadband grants and loans that are in the stimulus bill. So a lot of us are just concerned when you point out that it is not capped and may increase significantly.

I guess another question would be to you: Do you think this fund will likely shrink? Can you say categorically “yes” or “no”?

Ms. MATTEY. Are you speaking about the High-Cost Fund?

Mr. STEARNS. The whole fund.

Ms. MATTEY. The whole fund. I do not believe the whole fund will shrink.

Mr. STEARNS. I think that is fair to say.

Ms. MATTEY. We submit our projections to the Office of Management and Budget. And our projections show that, over time, the fund will grow.

Mr. STEARNS. You are saying including under the bill, too?

Ms. MATTEY. I was referring to our projections that we submit, as required by law, to the Office of Management and Budget, you

know, indicate that the fund overall will grow. And that is a matter—

Mr. STEARNS. Under this bill and under what you said, did you come up with a quantitative amount that you thought it would increase by?

Ms. MATTEY. No.

Mr. STEARNS. Did you have any projection at all?

Ms. MATTEY. We have not done an in-depth analysis of the specific provisions of the bill.

Mr. STEARNS. OK. What is your definition of an underserved household? Does that include wireless as well as land lease?

Ms. MATTEY. I would view, personally, an underserved household would be a household that has some form of broadband but perhaps does not have broadband of the speed that we are aiming for in the future. So it is a household that is beyond dial-up but perhaps does not have as robust a speed as we want as our goal.

Mr. STEARNS. Mr. Chairman, I don't see any clocks here, so I don't know how much time I have left or not.

Mr. BOUCHER. Well, it is one of the technical malfunctions we have here this morning. We are sort of beset with them. Actually, the Health Committee should have been having this room. Well, anyway, that is an intramural debate for another day.

Mr. STEARNS. Well, I will just finish up with—

Mr. BOUCHER. You actually have a few more seconds.

Mr. STEARNS. Oh, OK.

Well, let me just ask each member of the panel if there is anything in the bill they would change, delete, or add. And just start with you, Ms. Matthey, and just work to my right.

Ms. MATTEY. Well, you know, the FCC has not taken a formal position on the bill or any of the provisions—

Mr. STEARNS. I am not asking for a position. I mean, is there anything you would change? I mean, just any dot or comma or colon you would change? Anything in this bill you would change?

I mean, you have indicated that it will increase significantly. I assume you would like to put some language that would say that it can't go up and that the money has to be actually reduced.

Ms. MATTEY. Actually, there is one area that the bill doesn't really address, and that is the role of States in our shared Federal-State responsibility for universal service. And I would note that Nebraska actually has gone through the process of doing rate rebalancing and has established a State high-cost fund which supports the provision of service to carriers in that State.

So that is an area that, you know, I don't see addressed in the bill, and I think it is something we certainly have been thinking about at the FCC.

Mr. STEARNS. OK.

Mr. McCormick?

Mr. MCCORMICK. Well, there are a number of things that would sweeten the package for us. But, as I said, we know that this is a delicately balanced package, and we urge its package.

Mr. STEARNS. OK.

Ms. Bloomfield?

Ms. BLOOMFIELD. We also support the delicate balance. I would say cost models are difficult. What works in Montana doesn't necessarily work in Alaska.

Mr. STEARNS. Mr. Davis?

Mr. DAVIS. I think I am in the same place, in that, as a package, we support it. Are there things we would write differently? Sure, but is that going to cause some other component of the bill to fall apart?

Mr. STEARNS. Ms. Grillo?

Ms. GRILLO. I think we have concerns about the contribution system as it exists today and a revenues-based system. You know, in a perfect world, perhaps we would support language that would move away from revenues and move closer to a numbers- or connections-based system.

Mr. STEARNS. Mr. Assey?

Mr. ASSEY. I would echo what my other colleagues have said. It is obviously a package. Obviously, we are very concerned about the cost controls, but we are comfortable with the bill as it stands.

Mr. STEARNS. Thank you, Mr. Chairman.

Mr. BOUCHER. Thank you very much, Mr. Stearns.

I would just note that our legislation only addresses the High-Cost Fund. It does not address the balance of universal service. So any thoughts about the overall fund perhaps growing really are not relevant to this specific legislation per se.

The gentleman from Pennsylvania, Mr. Doyle, is recognized for 5 minutes.

Mr. DOYLE. Thank you, Mr. Chairman.

I want to talk a little bit about paying for the USF by charging a fee for telephone numbers, this numbers approach. So I have three questions, and I am just looking for "yes" or "no" answers. But, I mean, it is not the SATs. You could say "maybe" or "I don't know." And I am exempting Ms. Matthey from this. I just want to ask the five witnesses. So I will state the three questions first.

First, universities have hundreds, often thousands, of direct-dial phone numbers. A group of university IT professionals have filed a letter at the FCC saying that if the numbers approach replaced the current USF funding mechanism, their USF bill would increase tenfold, meaning they would have to take out telephones in dorms and bus shelters, making their campuses less safe. Can you understand why universities would seek an exemption for their numbers or face the prospect of ripping out their emergency call boxes?

Secondly, some but not all electronic book readers, like Amazon Kindle, have telephone numbers. And that is because they wirelessly download new books via a Sprint cell connection. Now, Sony readers make you sync the reader to a PC via wifi. Can you see why a company like Amazon would have to eliminate this feature unless it can get an exemption to pay into the fund because their competitors wouldn't have to?

And, third, there are companies in my district, including Contact One Communications, that need thousands of numbers to sell services like call centers and telephone answering. Does it make sense that they would seek an exemption for their tens of thousands of numbers or risk paying tons and tons of new money to the Universal Service Fund?

And maybe we will just start with Mr. McCormick and just go right down right down the line, "yes," "no," "maybe," or "I don't know."

Mr. MCCORMICK. Well, first of all, yes, I understand the concern. But the legislation provides flexibility to the FCC in addressing those connections.

And I would say that, in each and every one of those cases, particularly, like, the university telephones, universities are using those telephones to call into rural areas. I mean, the whole theory is that the utility of a telecommunications network, the utility of a broadband network is based upon—

Mr. DOYLE. Yes, but not for call boxes, certainly.

Mr. MCCORMICK. But what the legislation does is to provide flexibility so that they can use IP addresses, they can use telephone numbers, and they can take into account these kinds of, sort of, like, large call boxes.

Mr. DOYLE. Ms. Bloomfield?

Ms. BLOOMFIELD. We have historically supported a revenue-based assessment, which we have just found to be a little bit easier. But I do think the important part is looking to expand the base so you limit some of the pressure there.

Mr. DOYLE. Mr. Davis?

Mr. DAVIS. Yes, no, no.

No, I agree with Mr. McCormick, in that I think the legislation provides flexibility for the FCC to look at various circumstances, but I think it has to be recognized, as you go from one method of collection to another, some are going to pay less and some are going to pay more. It is just going to have that effect.

Mr. DOYLE. Uh-huh.

Ms. GRILLO. Yes, I mean, we agree that, you know, there are going to be concerns on all sides if you shift from revenues to numbers. And there has been a lot of talk, obviously, from universities and libraries.

I guess what we would say is, the FCC has to keep in mind that the more exemptions there are, the higher the per-number charge or the per-connection charge would be. And that, you know, can be borne by consumers, by small-business owners. So that is just a consideration that I think the legislation would permit the FCC to take into account.

Mr. DOYLE. Uh-huh.

Mr. ASSEY?

Mr. ASSEY. Yes, I understand, and I agree it is exactly the sort of thing the FCC ought to be empowered to work through, for the reasons that Kathy articulated, because the more exemptions you have, the higher the per-number charge.

Mr. DOYLE. Yes, I mean, I think in these cases, Mr. Chairman, there is a good case to be made for a carveout, you know, in this numbers approach. But if the premise is that numbers is a cleaner way to do it, then the carveout sort of make it unclear. So perhaps we should just fix what is wrong on the contribution side by improving the revenue model instead.

Let me ask Ms. Matthey, I have questions about the requirement in the bill that recipients of the Universal Service Fund provide broadband. Now, I wholeheartedly agree with that requirement,

and I appreciate Mr. Boucher adding it. However, some witnesses state that waiver provisions are needed to ensure that recipients of Federal money won't have to provide broadband where it is most economically difficult. The bill would automatically grant waivers where the cost of deployment is more than three times the national average.

Ms. Matthey, can you tell us, of the parts of America that aren't connected to broadband, what percentage of those would cost more than three times the national average to connect?

Ms. MATTEY. I can't answer that question definitively because we don't have complete information at this time to do that.

I can say, based on extrapolating from our existing cost information that we have about, under our current rules, the provision of universal service for voice service, it looks like, ballpark, perhaps 1 to 2 percent might be over that 3 percent threshold.

Mr. DOYLE. Uh-huh.

Ms. MATTEY. So it would be a situation, you know, where you would presumably be able to extend broadband to roughly two-thirds of the unserved. But there may be, you know, a quarter of the unserved that are still not served with such a waiver provision.

But I really caution you that that is very much of an estimate and we don't have the information.

Mr. DOYLE. But is it fair to say it is the FCC's intent to look at the potential impact on your ability to require carriers to deploy broadband services to unserved areas on this? I mean, if we want to make sure that everyone that is getting this money deploys broadband, obviously what I am hearing is that is not going to happen, in some cases.

Ms. MATTEY. Well, obviously, we would defer to the direction from Congress as to, sort of, how far we should go. Everybody recognizes that it is very, very expensive to extend service to that last percent. And we would follow the lead wherever Congress tells us to draw the line.

Mr. DOYLE. Uh-huh.

Mr. Chairman, thank you. I think I have used my time.

Mr. BOUCHER. Thank you very much, Mr. Doyle.

The gentleman from Nebraska, Mr. Terry, for 5 minutes.

Mr. TERRY. Thank you.

A couple of observations. First of all, on the revenue side, the requirement that if your service is primarily voice, that you would contribute, understanding there would be a variety of technologies, one where you probably have to use a revenue model and maybe another type of technology model where the numbers model makes better sense, so we give that level of flexibility to the FCC so they can determine which is the appropriate mechanism for the revenue.

And is that an adequate flexibility for the FCC, Ms. Matthey?

Ms. MATTEY. We very much appreciate the flexibility in this legislation.

Mr. TERRY. All right. Thank you.

Ms. Bloomfield, in that regard, is your constituency oK with that?

Ms. BLOOMFIELD. Absolutely. I think the hybrid approach might be the one that makes the most sense. And we have been working

closely with others in the industry and the FCC to, kind of, figure out what that forward-looking model is going to be on that.

Mr. TERRY. Ms. Grillo, you are the only one that seemed to be opposite of the flexibility.

Ms. GRILLO. Well, we are not opposite of the flexibility. I think we just—we have had a concern for a long time about the current system, and it really gets more intense every year just because the idea that you can separate information services from telecom services just gets more challenging every year.

So we do appreciate the flexibility. And, obviously, you know, the FCC is the expert agency and should be making these determinations. But we do feel strongly that the time is now to move toward a more objective numbers-, connections-based contribution.

Mr. TERRY. Thank you.

Back to you, Ms. Bloomfield. I am going to give this question to you because, frankly, it is your constituency that we started this process, to give them some level of certainty that the fund that they rely upon to provide services to the high-cost rural areas will exist in the future. There has been great concern about the cost-containment measures in here. And most of those cost-containment mechanisms in here really directly affect your constituency. And so I want to direct this question to you.

And, first, before I make the question, we started this with a cap, and the cap was criticized. Your constituency opposed it pretty passionately. But we have gone to a different model where we specified the cost containment. Now the same people that criticize the cap are criticizing this mechanism now, which is a little frustrating to me.

But I want to ask you, specifically, what are the cost-containment provisions in here, and how will they affect your constituents?

Ms. BLOOMFIELD. Thank you for asking the question.

I think, you know, when you look at the cap, I think part of the thing—you almost have to go back to what Congress and what policymakers really want to achieve. And if you are really talking about universal broadband to all Americans, let's be clear, it is going to be a costly proposition. But I think the payback in the long run, you know, getting this country being broadband-deployed, is going to be very, very important for us moving forward.

So I think it is hard to actually say, when you look at a cap and you say, well, what would the actual cap be, what would the cost be, what is the cost of getting broadband out there everywhere? And I think you have the pieces with the stimulus funding from NTIA and RUS going out the door; you look at the USF support. So I think there is kind of an unanswered question about what exactly that cost is.

I think until you, kind of, look back at that and you, kind of, look at how do you expand the base, that you are including as many folks contributing as possible, I think a hard cap is very, very difficult.

If you are in the process and you look at the waiver provision and you have that last 3 percent of your service territory that you need to build broadband out to but you are not quite sure what the cost is going to be because those customers are out on a very long

loop, the cap is really going to stop some of that investment, and I think particularly at a time when you really want to be giving incentives for investment.

Mr. TERRY. Let me guide you towards the cost-savings measures that are in—

Ms. BLOOMFIELD. That are in the bill, OK. Let's do that.

Mr. TERRY [continuing]. This current version. And is that adequate for Mr. Stearns to have some level of confidence that this is not going to explode?

And I guess we received this copy last night from the FCC, and I got it a few minutes ago, but, "The High-Cost Fund, not capped, may significantly increase." I mean, our whole attempt was not to increase this. So, evidently, the FCC has said that we failed in that, but I think they misunderstand.

Ms. BLOOMFIELD. And I think there are a lot of provisions in the legislation that ensure. You know, I think when you look at how you are actually distributing the money, I think the effort in terms of the competitive bidding with the wireless providers, the multiple ETCs, has been something that I think the entire industry has, kind of, watched with frustration for a long period of time.

I think that, as you look at more competition in some of these markets, I think you are going to see some of the declining costs. So I don't think you are going to see the explosion that has been projected. And, again, you know, you can't put a number on it because a number is hard to come up with.

Mr. TERRY. Mr. Assey, some of the cost-containment measures that you all brought forward to us have been adopted. Are you comfortable that those will actually be cost-saving measures?

Mr. ASSEY. We are comfortable and hopeful that they will. You know, we live in a world where competition is not a static entity, and one of the most important things, I think, from our perspective, that this bill does is adopting a permanent and ongoing mechanism so that, as competition extends and we are able to provide broadband service in areas without support, we are not essentially picking one competitor versus another.

Mr. TERRY. Right. I think that made sense, too.

My time is probably way up, so I yield back.

Mr. BOUCHER. Thank you, Mr. Terry.

We have a series of recorded votes pending on the House floor, and we have about 8 minutes to respond to those roll-calls. I think we probably have time for Ms. Matsui to propound her questions. I don't think we are going to have time for the other two colleagues to ask theirs. And Mr. Space says he is going to waive questions. I know Mr. Stupak has some questions.

I am going to propose that we have Ms. Matsui's questions, and then we will ask you to wait, if you will, and we will come back for further questioning subsequently.

Ms. Matsui?

Ms. MATSUI. Thank you, Mr. Chairman.

As I mentioned previously in my opening statement, there are far too many households who just simply cannot afford broadband service. The USF low-income fund was created to ensure that qualified lower-income Americans living in urban areas and rural

areas have a program where they can access affordable telecommunication services.

As we promote the transition of USF from telephone service to broadband services, the USF low-income fund is a vehicle to ensure all Americans living in urban and rural areas have equal access to at-home broadband services. My legislation to expand the USF Lifeline Assistance program for universal broadband assistance adoption will ensure that transition from telephone service to broadband service is a reality for these low-income households.

A question for Ms. Matthey: In the recent FCC broadband adoption survey, did the FCC find that the price of broadband service and related installation costs is a main reason why lower-income households do not subscribe to the Internet?

Ms. MATTHEY. The survey indicated that typical non-adopters face multiple barriers, but cost was the one most frequently cited.

Ms. MATSUI. With respect to any broadband Lifeline pilot program, would it be the intent of the FCC to administer the program to ensure that eligible low-income consumers in both urban and rural America have an equal opportunity to participate in the program?

Ms. MATTHEY. Oh, absolutely.

Ms. MATSUI. OK. What are some of the factors that the FCC will consider to ensure a cost-effective Lifeline/Link-Up program for broadband?

Ms. MATTHEY. Well, we hosted a roundtable discussion about Lifeline in June, and we solicited information from a variety of stakeholders about how to effectively design pilots to test the provision of that subsidy for broadband.

And we hope to very much also learn from the results of the BTOP awardees that will be announced and finished very, very soon, in the next week or 2.

Ms. MATSUI. OK, that is good to know. Thank you.

Questions for Ms. Grillo and Mr. Assey: From an industry standpoint, what are some of the factors you would encourage the FCC to consider in implementing such a Lifeline/Link-Up pilot project?

Ms. GRILLO. Well, we have been involved in a pilot program similar to what you have described. Some of the other factors, other than cost to a consumer, may be relevance. Some consumers, you know, don't see the relevance of broadband in terms of their everyday life. Some of it may have to do with security: concerns about the security of a connection and the information transmitted over it, concerns about children and what children do online.

So a lot of what we have tried to focus on in terms of a pilot is an examination, today, what really does drive consumers and what the government can include in a Lifeline-type program that would actually address all of those issues, not just price or cost. But, obviously, that is a concern for a lot of people.

Ms. MATSUI. Well, also, digital literacy.

Ms. GRILLO. Exactly.

Ms. MATSUI. OK.

Mr. Assey?

Mr. ASSEY. Yes, thank you for the question. This is obviously an area where the cable industry has done a lot of work, as well, and

we are proud to support your bill because we do think it is on target.

The cable industry developed an A-Plus program to really focus on this adoption problem, because we recognize that even though the cable industry can provide service to 92 percent of households, there are a lot of people who could get it who don't.

What Ms. Matthey said, the data that was collected and talked about why people don't adopt broadband covered many factors. And we, kind of, focused on three, digital literacy probably being chief among them. And our program is designed to focus on middle-school children and really try to educate them about safety, security, privacy, and make them comfortable with being in a digital environment.

The other point I would raise, when we talk about cost, I think we need to look at that factor a little bit more discretely, because, unlike the situation with telephone service, one of the biggest gating factors in cost is actually the cost of the computer, not necessarily the cost of the service. And the data actually reflects that.

So, focusing on the hardware, focusing on the service, focusing on the digital literacy, that coordinated approach will give us our best chance at success.

Ms. MATSUI. OK, thank you.

Ms. Bloomfield, in your view, would a Lifeline program for broadband increase adoption rates in rural America?

Ms. BLOOMFIELD. Absolutely. We think it goes really hand-in-hand with what the High-Cost Fund is already doing in terms of the deployment in rural America. So, the same incentives. We have the same issues in rural America as urban American does with low-income households.

Ms. MATSUI. Thank you.

And a final question for Ms. Matthey: How long, in your view, does the FCC believe it will need to conduct pilot programs to gather the appropriate information required to develop the most cost-effective program possible?

Ms. MATTHEY. We are still working on that internally. We have had a series of meetings with various interested stakeholders. And in the course of those meetings, some have suggested, you know, 1 year, 2 years, 3 years. Some have suggested things shorter and some longer, so we are still working on it.

Ms. MATSUI. I think my preference would be to have something shorter.

Thank you very much. I yield back.

Mr. BOUCHER. Thank you very much, Ms. Matsui. And we look forward to working with you on a broadband Lifeline provision. And I want to commend you for bringing that very well-developed idea before the subcommittee.

The gentleman from Florida, Mr. Stearns, is recognized for a unanimous consent request.

Mr. STEARNS. Unanimous consent, Mr. Chairman, that the FCC's report, "Comparison: Universal Service Fund Transformation Recommendations, August 2010," be part of the record.

Mr. BOUCHER. Without objection.

And we stand in recess until the conclusion of these votes.

[Recess.]

Mr. BOUCHER. I would like to ask our witnesses to resume at the witness table, please. Sorry for the delay. Thank you for your patience.

At this time, I am pleased to recognize the gentleman from Michigan, Mr. Stupak, for 5 minutes.

Mr. STUPAK. Thank you, Mr. Chairman. We thank you, and we thank our witnesses for staying with us so we could ask a round of questions.

First, Mr. Chairman, let me thank you and Mr. Terry for putting forth this legislation. It is a pretty good piece of legislation.

As I mentioned to you as we are walking down to votes, I still have concerns I have raised before in this committee and I continue to raise because it is an issue we have to deal with, and that is—while you mentioned public safety on page 10 of the bill, we don't talk about a public safety network, specifically public safety and interoperability broadband network. And I would certainly hope there would be some way we could work this out. Ms. Matsui talked about a lifeline, but there is no greater lifeline than having interoperability for our first responders, whether it is an ambulance, a police officer, or a firefighter. We do need that, and I hope there would be a way we could work that out. I know this bill has been put together carefully, and it might be hard to do it, but let's continue to explore possibilities.

With that, let me ask Ms. Matthey a question, if I may. In your testimony, you note that, and I quote, "We should be looking at ways to target support only to those areas that really need it, to deploy and sustain broadband networks capable of providing high-quality broadband and voice services."

So my question is, how would you or the FCC determine—or what factors will the FCC use to determine which areas need support and which areas don't need support?

Ms. MATTEY. Ultimately, the goal of universal service is to provide economic support to areas where there is no private-sector business case. So, in order to target support, one would look at the areas and determine whether or not, you know, there are multiple providers in that geographic area that are providing service without support and, conversely, is there only one provider in a particular area. So you need to look at, sort of, who is in the marketplace and figure out, from a business case perspective, where you need to add that supplemental investment coming from universal service.

Mr. STUPAK. You said a private provider, so if that provider in that area is a municipality, would you still consider that an underserved area then?

Ms. MATTEY. That is an interesting question I haven't really thought about. I am not aware of any municipalities that are actually providing voice service. And, obviously, we want to make sure that consumers continue to have voice service as well as broadband.

Mr. STUPAK. Well, let me ask you this because you brought it up and also Ms. Grillo brought it up. You mentioned the importance of ensuring that the burdens on the consumer never outweigh the benefits in the mission to provide support where it is needed.

So where is the tipping point? When does the burden outweigh the benefits? Where is that point? Have you thought about that? Have you kicked that around at the FCC?

Ms. MATTEY. I have been thinking about that for a very long time.

Mr. STUPAK. And your answer is?

Ms. MATTEY. I wish someone would give me the answer.

Mr. STUPAK. Well, that is a valid point. And we talk about these concepts, but we have to—you know, what factors are we going to take into consideration to find what is the tipping point?

Ms. MATTEY. Right. I mean, ultimately, it is a political judgment, you know, and it is a collective judgment as a society. And we very much, you know, will take whatever direction Congress, you know, gives us in terms of deciding where that balance is.

But, ultimately, you know, the point of the testimony was just to remember that consumers contribute to universal service as well as receive the benefits.

Mr. STUPAK. Well, let me ask you this question then. In Ms. Bloomfield's testimony, she points out that the FCC is in charge of determining the process for areas of losing or re-obtaining universal service support. Has the FCC thought about how they will develop the rulemaking for losing or re-obtaining?

Ms. MATTEY. I am sorry, was that a question to me? Are you referring to what she said?

Mr. STUPAK. To you. Ms. Bloomfield brought it up in her testimony, and I thought it was interesting. So has the FCC thought about how are you going to do this? What is the process for areas to determine if they are losing or re-obtaining universal service support?

Ms. MATTEY. I am not sure I completely understand the question. I apologize.

Mr. STUPAK. Ms. Bloomfield, do you want to elaborate a little bit on that? It was your testimony I am citing.

Ms. BLOOMFIELD. I think Congressman Stupak is referring to, you know, what happens as access lines are decreasing—

Mr. STUPAK. Right, decreased.

Ms. BLOOMFIELD [continuing]. And, you know, the impact of the line loss and what that does to the ultimate support that some of the providers are receiving today.

Ms. MATTEY. Right. Well, under the current system for the smaller rate-of-return companies, as they lose lines, the amount of support per line they receive will go up under the existing support program, because that is designed to ensure that the small rate-of-return companies recover the fixed costs of their network regardless of how many customers actually choose to subscribe from that provider.

Mr. STUPAK. OK.

Mr. Davis, in your testimony, you point out that 14 million people living in 7 million housing units in the United States do not have access to broadband infrastructure. You go on to stress the importance of directly and explicitly supporting broadband service.

Do you think the goal of providing broadband to unserved and underserved areas can be realized if the high-cost funding is reduced?

Mr. DAVIS. Do I think it can be realized if all high-cost—

Mr. STUPAK. Yes, if we start reducing high-cost funding.

Mr. DAVIS. I think it depends over what period of time and whether you are talking about 100 percent coverage, as has been discussed. That gets extraordinarily expensive, and so we would have to look at that. But certainly—

Mr. STUPAK. Right. I am in one of those very expensive areas.

Mr. DAVIS [continuing]. We can do a much better job of providing broadband support than we do today, and we can get broadband to a far higher percentage of customers than we do today with broadband support.

Mr. STUPAK. But if we reduced the high-cost funding, of course we would leave more and more areas behind, right?

Mr. DAVIS. I think we can make the current high-cost coverage much more efficient, as is anticipated in the bill, by reducing support to wireless carriers in areas that really do not deserve support.

Mr. STUPAK. OK.

Ms. Grillo, let me ask you this. In your testimony, you highlight the growing problems of traffic pumping and the urgent need to put a stop to the scams. You also mention that the Universal Service Reform Act will cut off many of the traffic-pumping scams.

Do you think the bill's language is strong enough to put an end to traffic pumping, or is there more we need to do?

Ms. GRILLO. I think the language is strong enough to stop many, if not all, of the problems that we are seeing right now, yes.

Mr. STUPAK. OK.

Ms. Bloomfield, if I may, in your testimony you raise concerns about small rural telecommunication providers. Specifically, you point out the provisions that call to reduce or eliminate high-cost support in competitive areas.

Rural areas make up a large part of my district. Can you please elaborate on the problems you foresee in rural areas if high-cost support were eliminated?

Ms. BLOOMFIELD. Part of the problem is, when you talk about high-cost areas and whether or not they are competitive, a lot of that is going to depend on how you define "competitive."

So let's say, for example, a carrier is able to build out to 98 percent of their service territory which is a very high-cost area but, you know, not able to, kind of, always get—you have, kind of, the doughnut and the hole, so it is very expensive to get to those outer regions.

So when you look at competition, you know, is your competitor going to come in and actually provide service to just that center of the hole where you actually have that density and where it is actually a lower cost to be competitive? That leads to the question of what happens to those consumers at the very far reaches where it is very expensive to reach them.

And the incumbents right now have the carrier-of-last-resort obligation.

Mr. STUPAK. Right.

Ms. BLOOMFIELD. So those carriers have to go out, regardless of the cost. So the problem is, if you kind of cut out the middle where it is ripe to be competitive, all you are doing is increasing the cost on the fringes.

Mr. STUPAK. Nothing, further, Mr. Chairman.

Thank you. Thank you all for your testimony.

Mr. BOUCHER. Well, Mr. Stupak, thank you very much for your thoughtful questions.

Thanks again to our witnesses. I appreciate your very positive testimony today.

Ms. Matthey, thank you for your informative testimony, coming from the Commission. I appreciate your attendance.

I would simply note, in closing, that we have substantial savings that are contained within this legislation. Moving to competitive bidding on wireless, according to Ms. Grillo, saves between \$200 million and \$500 million every year, in terms of High-Cost Fund expenditures. We deny support in areas where there is competition in the offering of voice-based telephone service. That will result in savings, although we don't have a hard number on that. We address traffic pumping, which, in turn, is going to result in savings. And we say that net revenues from all supported services will be considered when determining the appropriate level of support.

All of these are provisions that will result in savings from the High-Cost Fund. I felt compelled to note that, given some of the questions and comments that came forward this morning.

Well, I want to thank everyone. This has been a very productive hearing. And we will have further proceedings on universal service.

That said, this hearing is adjourned.

[Whereupon, at 12:27 p.m., the subcommittee was adjourned.]

[Material submitted for inclusion in the record follows:]

Statement of
Representative John D. Dingell
Committee on Energy and Commerce
Subcommittee on Communications, Technology, and the Internet
Hearing on "H.R. 5828, the Universal Service Reform Act of 2010"

September 16, 2010

Thank you, Mr. Chairman. I commend you and Mr. Terry for your work on H.R. 5828, the Universal Service Reform Act of 2010.

Put simply, advances in telecommunications, the changing preferences of consumers with respect to such services, and a decreasing funding base have made it necessary for the Congress to re-examine the policy goals and functioning of the Universal Service Fund. Universal service mandates must be modernized with respect to these developments in order to ensure all Americans, regardless of geography or income, have access to high-quality telecommunications at affordable rates.

As I have suggested in the past, three principles should guide our efforts in this matter. First, all providers of telecommunications should contribute equitably to support universal service. Second, all communications – and not simply *interstate and foreign* communications – should be subject to assessments to support universal service. Finally, we should not play favorites with new communications technologies when it comes to Universal Service Fund contribution requirements, because this will have the undesired effect of shortchanging the Fund, as well as amounts to the picking of winners and losers in the marketplace. I am pleased to see that H.R. 5828 incorporates these principles and, moreover, that the bill recognizes broadband as a universal service and makes provisions to support the expansion and maintenance of its infrastructure.

Mr. Chairman, I thank you for your courtesy and commend you and Mr. Terry for the congenial, bi-partisan work that has produced the bill we consider here today. It is well written and enjoys wide support across an array of stakeholders. As such, I wish to add my name as a co-sponsor and urge you to maintain the fine balance you have struck in this legislation.

I yield back the balance of my time.

**Statement of Anna G. Eshoo for the Record
At the Communications, Internet and Technology Subcommittee
On the Universal Service Reform Act of 2010
September 16, 2010**

REP. ESHOO: Thank you, Chairman Boucher, for holding this hearing today. To the average American, Universal Service Reform may seem a very technical topic. But this topic has very important implications. I believe it can be a valuable tool to improve and enhance access to broadband services across the country.

We all pay a Universal Service Fee, to ensure that communications services are available to everyone, including in places that are hard to reach, and for people who might not be able to afford service. In the 1930s, this was meant to ensure that carriers would provide rural homes with telephone service even if it was difficult or expensive to do so.

Telecommunications have come a long way since then. We need to ensure that the Universal Service Program lives up to its name and provides essential telecommunications services to all Americans. Today, essential services should include broadband.

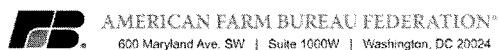
The National Broadband Plan recognizes that extending broadband service raises the same challenges that telephones faced nearly a century earlier. They recognized that USF could be a powerful tool to ensure that all Americans had access to broadband. In order to do so, we need to change the old way of doing business.

I appreciate the effort that the Chairman and Mr. Terry have put into this bill, and their commitment to using USF as a broadband deployment tool. But I have heard many concerns about the bill. It would bind the FCC's hands in their implementation of USF reforms in the National Broadband Plan. Indeed, some of the organizations testifying today praise this bill precisely because the bill "redirects" the plan's efforts on USF.

Further, the bill retains support for legacy technologies without imposing sufficient obligations to increase broadband support. It eliminates many free or below-cost teleconferencing services that consumers have come to rely on. It does not expand the Lifeline or Link-up programs to ensure that low-income families have access to broadband. It does not reform the E-Rate program to ensure that schools and libraries have access to broadband.

In addition, we must ask about the obligations for carriers who receive this money. The BTOP grants program in the Recovery Act, which I strongly supported, required the recipients to abide by non-discrimination principles for net neutrality. We included that language because public funds come with public obligations. Over 2,000 applicants sought BTOP funds, and were willing to live by those terms. We should include similar language here. This should not be a giveaway to corporate interests to spend however they please. This is taxpayer money, and we have every right to require the recipients to abide by some rules of the road.

I hope this hearing will be able to address the many concerns that have been raised.



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September 14, 2010

The Honorable Rick Boucher
Chairman
Subcommittee on Communication,
Technology and the Internet
2125 Rayburn House Office Building
Washington, DC 20515

The Honorable Cliff Stearns
Ranking Member
Subcommittee on Communication,
Technology and the Internet
2125 Rayburn House Office Building
Washington, DC 20515

Dear Chairman Boucher and Ranking Member Stearns:

The American Farm Bureau Federation believes that high-speed broadband services have great potential to bring opportunity to rural Americans. Farm Bureau represents more than 6 million families who live and work in rural America, many of whom do not have the same access to educational, medical, business and government services as Americans living in more populated areas.

H.R. 5828, the *Universal Service Reform Act of 2010*, has the potential to correct this inequity by declaring broadband a universal service, which allows for direct support from the Universal Service Fund (USF). Farm Bureau agrees that the USF should be used for long-term broadband deployment.

Many farmers and ranchers conduct their business operations from their homes. As government agencies increasingly rely on information technology to disseminate and collect information, affordable, high-speed, home-based broadband connectivity is becoming a necessary tool for producers. Farmers and ranchers without access to affordable high-speed internet connections might eventually be unable to comply with government regulations, take advantage of government services or gain market information. Therefore, affordable home broadband access is especially important to keep American agriculture competitive in a world marketplace.

America's farmers and ranchers need viable rural communities to supply the services needed to support their families and agricultural operations. To thrive, rural areas need access to health care, government services, educational and business opportunities. For many rural communities access can only be gained by using broadband services and sophisticated technologies that require high speed connections. Rural business owners need access to new markets and well-educated employees for their businesses. Rural health care providers need access to health information technology. Rural students need access to educational resources and continuing education opportunities. Current and future generations of rural Americans will be left behind their fellow citizens if they are without affordable high-speed broadband service to tap into health care and educational services, government agencies and new business opportunities.

Affordability is a critical component to broadband use in rural America because rural household incomes are typically lower than those in more populated regions of the nation. In rural areas where broadband service is available, our members have reported that the service is beyond the financial means of many residents of their communities. The development of a new cost model for universal support, which is part of this legislation, will ensure that the cost to the consumer is affordable.

Farm Bureau calls on Congress to join us in making a commitment to revitalizing our rural communities and ensuring the health and welfare of present and future generations of rural Americans by enacting H.R. 5828, *Universal Service Reform Act of 2010*.

Sincerely,

A handwritten signature in black ink, appearing to read 'Bob Stallman', with a long horizontal flourish extending to the right.

Bob Stallman
President

CC: Members of the Subcommittee on Communication, Technology and the Internet

HENRY A. WAXMAN, CALIFORNIA
CHAIRMAN

JOE BARTON, TEXAS
RANKING MEMBER

ONE HUNDRED ELEVENTH CONGRESS
Congress of the United States
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COMMITTEE ON ENERGY AND COMMERCE
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Minority (202) 225-3841

October 20, 2010

Carol Matthey
Deputy Chief, Wireline Competition Bureau
Federal Communications Commission
445 12th Street, SW, Room 5-C352
Washington, DC 20554

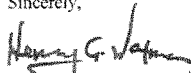
Dear Ms. Matthey:

Thank you for appearing before the Subcommittee on Communications, Technology, and the Internet on September 16, 2010, at the hearing entitled "H.R. 5828, the Universal Service Reform Act of 2010."

Pursuant to the Committee's Rules, attached are written questions for the record directed to you from certain Members of the Committee. In preparing your answers, please address your response to the Member who submitted the questions.

Please provide your responses by November 3, 2010, to Earley Green, Chief Clerk, via e-mail to Earley.Green@mail.house.gov. Please contact Earley Green or Jennifer Berenholz at (202) 225-2927 if you have any questions.

Sincerely,



Henry A. Waxman
Chairman

Attachment

The Honorable Cliff Stearns

- 1. During the hearing we submitted for the record an August 2010 document in which the FCC says that under H.R. 5828 the high-cost fund is not capped and “may increase significantly.” Which provisions in H.R. 5828 in particular does the FCC believe could significantly increase the size of the high-cost fund?**

As currently drafted, the bill gives the FCC the discretion to implement many key provisions, and the way that they are implemented could impact the ultimate size of the fund. Some of the choices that may increase the size of the fund include the extent to which the FCC may create a cost recovery mechanism in USF for intercarrier compensation revenues pursuant to Section 301(b) of H.R. 5828 and the provision in Section 103 requiring that USF support be calculated using wire centers for companies other than rate of return carriers. That section also directs the FCC, when developing the new cost model, to develop and implement a mechanism that maintains rate-of-return regulation for those companies subject to rate-of-return regulation at the time of enactment. Such a provision could lead to continued growth in the interstate common line portion of the high cost fund. Other changes, such as the provision in Section 105 requiring the elimination of section 54.305 of the Commission’s regulations, the so-called “parent trap” rule, which limits a carrier acquiring exchanges to the same per-line support the seller received prior to the transfer, may also increase the size of the high-cost fund.

- 2. Mr. Barton and I have said that we might accept a bipartisan compromise that expands the high-cost fund to broadband but ensures the high-cost fund does not grow, and preferably shrinks it. Can the FCC assure me that the high-cost fund will not grow if H.R. 5828 becomes law?**

No. Because of various factors, it is difficult to predict whether the high-cost fund will grow, and, as noted above, there are provisions in H.R. 5828 that could potentially increase the fund, depending on how they are implemented by the FCC. Also, it is particularly difficult to say how enacting H.R. 5828 as currently drafted will impact the size of the high-cost fund relative to the current projections. While several components (high cost loop and interstate access support) of the high cost fund are currently capped, other components (local switching support and interstate common line support) are not. Trends in high cost payments are difficult to predict, depending among other things on the extent of access line loss and investment patterns of companies that receive support based on their own cost submissions.

- 3. Are there any recommendations in the National Broadband Plan that the FCC could not adopt if H.R. 5828 became law? If so, what are they?**

The National Broadband Plan (NBP) recommended that the FCC eliminate all support provided to competitive eligible telecommunications carriers and use those savings, along with other savings, to establish a new Connect America Fund (CAF), which would ultimately replace the existing high-cost fund. The NBP also recommended that support under the CAF be limited to one provider per geographic area. If H.R. 5828 is enacted in its current form, Section 104(a)(4) would prevent the FCC from eliminating all support to competitive eligible telecommunications carriers, and it would also not be able to limit support to one provider per geographic area.

The NBP also suggested that the FCC identify ways to drive funding to efficient levels, including through the use of market-based mechanisms to award support based on neutral geographic units that are both company- and technology-agnostic. Section 104(a)(4) requires the FCC to establish competitive mechanisms to award support to mobile wireless communications service providers in areas where there are at least three such providers, but directs the Commission to maintain support at existing per-line levels in areas with less than three such providers, subject to adjustment under the interim cap. The net result of such provisions could be three supported providers in a given geographic area (one incumbent wireline provider and two mobile wireless providers.)

Further, the NBP suggests that the FCC consider using market-based mechanisms, where appropriate, to determine the firms that will receive CAF support and the amount of support they will receive. Section 103 requires the FCC to develop a model for incumbent carriers based on wire centers and study areas, which are geographies relevant to incumbent telephone companies. This provision potentially could preclude the use of market-based mechanisms for such companies.

